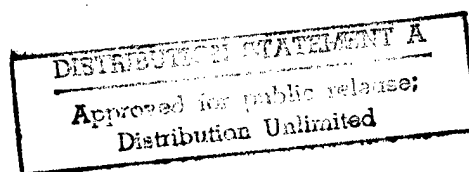


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3 FEBRUARY 1987

# Japan Report



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## JAPAN REPORT

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## POLITICAL AND SOCIOLOGICAL

### IMPACT OF MIYAZAWA'S APPOINTMENT AS FINANCE MINISTER

Tokyo ZAIKAI TEMBO in Japanese Oct 86 pp 242-251

[Discussion by political critic Kenzo Uchida, NIHON KEIZAI SHIMBUN reporter Akira Sakaguchi, Tokyo International University Professor Kosaku Nomura, and economic critic Manami Hirata]

[Text] Prime Minister's Motive for Taking In Miyazawa the "Biggest Obstacle"

A: Our topic for today is, What should we expect to see unfold in the economic policy of the postelection Nakasone administration, which now has 304 seats in the Lower House?--a policy that must, partly as a natural extension of the campaign promises but more importantly in view of the internal and external pressures that are likely to grow ever stronger, be centered on the expansion of domestic demand. I suggest we examine this question with the spotlight focused on former Chairman Miyazawa of the LDP Executive Council.

The matter of expanding domestic demand, in particular, of course has a bearing on the immediate counter-cyclical measures as well as on the mid- and long-term structural reform, but there is another matter which is of general concern to the people--it is the question of tax increase. While campaigning in the latest election, Mr Nakasone flatly declared that he would have nothing to do with the idea of instituting a large-scale indirect tax, even if it were recommended by the government Taxation System Council. Yet, judging from the way things are going in the wake of the election in which the government party won 304 seats, it seems to me that these election pledges are being violated with impunity.

Against this backdrop, when we consider the likely direction of economic management by the third Nakasone Cabinet now in place, the most interesting thing is that Mr Miyazawa, long known as an activist, has been installed as the finance minister and that, moreover, he himself has accepted such an appointment.

From the political standpoint, all sorts of comments are being made and no doubt Nakasone and Miyazawa have motives of their own. Of course I would like you to discuss this aspect as well, but there is one point which is largely being overlooked--that is, given the nature of the past relationship

between the finance bureaucrat and Mr Miyazawa, Mr Miyazawa's holding the finance portfolio has a very serious side to it in some respect.

Frankly speaking, Mr Miyazawa had long been regarded as a natural enemy for the Ministry of Finance. Now, with the same Miyazawa presiding over the very ministry, the question is, Will his appointment as the minister bring changes and adjustments to the views he had advocated while he was chairman of the party's executive council? This will be a point to watch when we view how the third Nakasone Cabinet handles economic management.

By way of a review, I would like to pose a question to Mr C: What should we make of the situation that surrounded Mr Nakasone's selection of Miyazawa for the finance portfolio and the latter's acceptance of the appointment--a question that has generated various political speculations in terms of the motives of the two principals involved.

C: The picture changed the minute the election produced a 304-seat victory for the LDP. Up until that time, Miyazawa had been the person whom Nakasone had not only found quite disagreeable but also felt the need to guard against. The moment the election victory emerged as a fact, however, Nakasone knew he would be at the helm for a while longer--that everything depended on his continued pitching. In that frame of mind, Nakasone faced the question of how to proceed with personnel assignments and came to the conclusion that nothing would be more fitting to his "great prime minister/party president" image than to have all three so-called new leaders serve under his command. It was his political decision.

Meanwhile on the policy side of the considerations, taking into account the somewhat changed attitude of the financial and industrial circles and knowing Miyazawa's past criticism of the Nakasone-style economic management and fiscal policy, Nakasone apparently decided to let Miyazawa have an opportunity to try his own way but with an implicit understanding that whatever he Miyazawa may try will be closely checked by him Nakasone, the great prime minister/party president. I believe this reading is not too far off.

To put it more bluntly, I suspect that Nakasone is trying to use Miyazawa as a tool for changing the financial and economic policy--make him a front man for now but replace him any time the situation calls for it. As they say, if things go well, the credit will go to the magnanimity of the great prime minister/party president; if not, the verdict simply will be that Miyazawa is not the right man for the finance portfolio, after all. This is about it, I think.

A: You said that Miyazawa was picked as a tool; if so, I wonder whether a policy shift is being planned. Do you think there will be a policy shift?

B: Not a fundamental shift but more likely a shift in moderation, I should think.

D: External factors weigh in heavily on this.

A: You mean the demands from external quarters including the United States?

D: Yes. The deciding factor is how powerful the external demand is going to be, don't you think? What is happening to the foreign exchange rate probably is a naked manifestation of this factor.

B: In the event of another wave of external pressure, I wonder what our government will do.

Further strengthening the yen would be the last thing the government would want to do. The government would not want to make investment in public works either. Even if investment in public works were implemented, the amount would not be large. It makes me wonder whether things are under control as they are.

D: Just now we have heard an analysis of the political motive on the part of the prime minister/party president. What about the motive of Mr Miyazawa who accepted the appointment?

C: For him it was a case of no-win situation--the prospects were bleak either way. So he opted to do the only manly thing in that situation, which was to find a way out of his predicament by going forward, not backward. I believe that was his political judgment. Being a man of considerable self-confidence, he does not consider the finance portfolio as a poor bargain. Rather, he is confident that he has the perfect blueprint for Japan's fiscal and economic management at this point in time, and if that is what they want him to do, he is ready to accept the challenge. He is being refreshingly open about this.

There were some people who played the intermediary role. Actually, all the political and policy considerations notwithstanding, Nakasone was unwilling to use Miyazawa, and Miyazawa, on his part, was advised by some of his men not to accept the cabinet appointment which, in their view, would be close to an act of unconditional surrender. That was when the intermediaries came into the picture: They asked Nakasone whether he had considered the national interest--interest from whose standpoint was a debatable point; they pointed out that, in spite of all the talks about the so-called new leaders, Miyazawa was the only one who had enough insight to do the job; and they concluded that it would be a folly not to utilize a man like Miyazawa. It worked, so they say.

A: A while ago Mr C said that if all goes well it will prove the man's caliber fit for a prime minister/party president, and that if not it will lead to the conclusion that Miyazawa was not the right man after all. Getting back to the meat of this observation...

C: Wait. When I said that if all goes well it will prove the man's fitness as a prime minister/party president, what I meant was that the credit will go to Nakasone.

A: I see. If things do not work out, it will be Miyazawa's fault.

C: Precisely. But that is not how Miyazawa looks at it. He believes that his good showing as the finance minister would lead nicely into his next step.

A: During the election campaign, when the party's Policy Coordination Council Chairman Fujio showed his true colors by mentioning something about making the question of large-scale indirect tax as an election issue, Mr Nakasone hurriedly denied it, going as far as declaring flatly that he would not institute such a tax even if it were recommended by the government's Taxation System Council. In truth, however, despite such a declaration, as soon as the election was over, the Taxation System Council came up with a new tax package proposal based on the "three types and four formulas" principle which, although not being referred to as a large-scale indirect tax, is in fact a new Japanese style indirect tax aimed at a broad segment of the masses. As we can see from this proposal, what has emerged openly and has become a subject of formal study which is already under way is the idea of raising the indirect tax as a means to introduce a new revenue source with which to compensate for a reduction in income and corporate taxes.

Should this indirect tax scheme go forward, it means that Miyazawa instead of being able to carry out much of the things which had been expected of him by the financial world, especially the leaders of the manufacturing sector hit hard by the negative impact of the strong yen, as well as by ordinary people on the streets who are also feeling the pains of the strong yen in more ways than one, would end up having to undertake something which the public does not want. Certainly this is a possibility. In fact some are saying that this is precisely the reason why Mr Nakasone picked Miyazawa for the job. Whether this is a valid view, I am not sure.

How Likely Is a Tax Increase?

C: Mr Miyazawa still believes a tax increase is impossible.

A: You have just touched on the subject about which I am most interested in hearing your views.

C: It cannot be done.

B: Cannot be done is right, indeed.

C: The so-called large-scale indirect tax cannot be instituted.

B: If they go for the "three categories and four formulas" route, the end result would be the spreading of the commodity tax for the manufacturing sector across the board, that's all. The point is, this would be a bad move, indeed.

A: That would be a taxation on goods leaving the warehouse.

B: Exactly--tax on goods leaving the warehouse. In short, it will be a tax levied on all goods such as beer. From the standpoint of the general public right now, the crucial question is how this tax would be applied to the

service sector. This is an important point from the standpoint of counter-cyclical measures as well. All this means that it would be a very bad tax.

I have the habit of putting forth an "ought-to-be such-and-such" kind of argument right off the bat; so, if you will bear with me, I think the answer to this whole question ought to be as follows: After all, the 304-seat victory was won on the promise of no large-scale indirect tax; therefore there ought to be none.

There is, however, another consensus among the people: They are saying that any major tax cut inevitably leads to a major tax increase. If that is the case, the problem is simple: I will say, let's forget about the tax cut, however regrettable this might be. By the same token, let's forget about the tax increase as well. Actually things were moving in this direction after Nakasone had said his piece on this subject. But then everybody jumped on him. For instance that fellow Takekazu Ogura, I must say he is an idiot. I am tempted to ask him face to face what kind of a nonsense he was talking about when he said, "There are three methods for doing it. Although we must respect the prime minister's view for what it is, we will proceed in our own way." If it is up to me, I will abolish the Taxation System Council.

I say so, but no one else--the mass media, the scholars and all--is saying anything like this. They let the tax reduction go as a foregone conclusion and then, as an afterthought, they fuss about what to do with the tax increase question. I still say the answer is simple: Let's do neither. That is the only solution.

To a degree, I think this idea has seeped into Mr Miyazawa's head. Granted the opposition party is a meager minority, but there is no way any full-blown indirect-tax proposal will pass the Diet. I do not believe the opposition is that helpless.

C: It has been only half a month since Miyazawa became the finance minister; I bet he is busily racking his brain on this question right now. He must be listening to the views of those finance bureaucrats as part of the process of putting his thoughts together at this very moment.

B: But the problem is, those finance bureaucrats are so eager to do something--anything. Their premise is that a tax reduction is a foregone conclusion; on that basis, they are dying to put through a tax-increase measure under some sort of subterfuge. After all, their sole purpose is to help Mr Nakasone. If someone says "Nakasone has lied," they say "No, it was not a lie--No, sir!"

I used to think rather highly of the man Nakasone, but I tell you he is finished as far as I am concerned--he is truly an outrageous fellow!  
(laughter)

A: While we are on this subject, let me offer some additional background materials for discussion.



In short, it is long known, on the basis of a potpourri of his remarks, that Miyazawa's image is that of an activist. Specifically, with regard to countercyclical measures and fiscal management, he has been an advocate of aggressive approaches. On the question of tax reduction, he favored giving precedent to a major tax cut and opposed the idea of effecting a tax cut with a matching tax increase simultaneously as envisioned by Nakasone. He said, for example, that large-scale reductions should be made in income and corporate taxes as a first step and that there should be no tax increases for about 3 years afterward. Only after some 3 years, some adjustments could be made to the tax structure to make it revenue neutral, according to him. In other words, observe how things go for about 3 years and then, if necessary, introduce a large-scale indirect tax or whatever--this was his "tax reduction first" argument.

Moving onto another subject: It is the problem facing the public works program. In the fiscal 1986 budget, 80 percent of the funds earmarked for public works has already been expended ahead of schedule, which means that the public works outlay will fall off dramatically in the second half of the budget year. This will cause an anxiety to many, and a supplementary appropriation must be arranged to alleviate such an anxiety. A revenue source must be found for that purpose. As a solution to this problem, Miyazawa suggested an increased issuance of construction bonds.

With regard to more and more government bonds coming to maturity which will have to be redeemed, Miyazawa questioned the necessity of cash redemption, suggesting as an alternative the idea of issuing new bonds to be used as refunding bonds. By so doing, he pointed out, the cash earmarked for bond redemption could be used for other countercyclical purposes. In sum, Miyazawa's position has been one of favoring an increased issuance of construction bonds, the redemption of matured bonds by the use of refunding bonds, the implementation of a tax-reduction measure as a matter of precedent and putting off the question of tax increase to be considered later.

That was what distinguished Miyazawa from Nakasone. Given Nakasone's position favoring a tax cut with a simultaneous and matching tax increase and the pursuance of a tight fiscal policy, these two men stood at the opposing ends of a policy conflict within the LDP administration. Now, with the emergence of Miyazawa--the man at one extreme--as the finance minister, the focal point of interest is how the differences between these men will be ironed out. Inasmuch as it was Nakasone who appointed Miyazawa, some even questioned just how far Miyazawa could go in exercising his own leadership and showing his own colors.

Now, a review of Miyazawa's more recent utterances following his assumption of the finance portfolio reveals that, on the question of countercyclical measures, he hopes to come up with supplementary budget plans for the public works program and at least a policy outline for the domestic-demand expansion measure during the month of September at the latest. Somewhat abstract, but that is what he has said. On the question of increased issuance of construction bonds, he has become ambiguous as reflected in his remarks "all in good time."

All this may be explained away by the simple fact that he just became the finance minister after all; nevertheless, clearly his remarks have become considerably more cautious than before.

It is on the issue of tax cut and tax increase where his position has definitely changed. He is now saying that if there is going to be a tax reduction effective fiscal 1987 there should also be a tax increase of equal proportion. To put it the other way--and to express it in the style of the Finance Ministry bureaucrats, he seems to be saying, "Increase the tax first and then follow it with a tax cut within the limit of that increase." All this is to take place beginning fiscal 1987 according to his basic plans. As for the large-scale indirect tax, the proposal by the Taxation System Council is likely to be used as the basis. Even though Miyazawa is not saying that he would use the council's proposal as the basis, he has indicated his support of the proposal.

Such being the case, one even gets the impression that, if anything, it is Miyazawa's activist position that has regressed somewhat and has come closer to none other than the policy line as mapped out by the Finance Ministry. Under such circumstances, other than the certainty that we will be hit with a tax increase, I doubt whether we will be seeing much of the positive aspects of the original Miyazawa lines reflected in the future policy execution.

Given the short time he has had as the finance minister, one should avoid making a hasty judgment about his performance; nonetheless, a comparison of his remarks since becoming the finance minister and those he made while serving as chairman of the party's executive council makes it quite clear that there has been a change in the Miyazawa mode, to say the least. One gets a strong impression that he has transformed himself from being an advocate of the cut-tax-first line to a supporter of the simultaneous and matching tax cut and increase policy and that he has become somewhat more cautious with respect to his call for aggressive fiscal policies.

Miyazawa Should Stick With His Own Tune

B: I do not have much of an impression one way or another. What Miyazawa has been espousing does not amount to much of a policy in the first place.

It is all very simple: He was calling for the issuance of construction bonds and refunding bonds as if he were talking about a magic of some sort. Actually what he was talking about was nothing more than withholding the redemption of one-sixth of matured bonds. The idea was to use the money so saved for stimulating the economy while slowing down the pace of fiscal reconstruction somewhat.

But in the presence of Mr Nakasone, Miyazawa's voice has been pretty well squelched. He now seems to be content with a more temperate course of action. Also, when all is said and done, he probably does not want to do anything that might hurt the feelings of those dear finance bureaucrats.

It is very interesting that some people are saying of late that cabinet ministers should use bureaucrats and not vice versa--which is something that goes beyond saying. If Miyazawa should say something like that, I will bet it will make things complicated for Mr Nakasone, if anything. (laughter)

D: If indeed Miyazawa has transformed himself as just pointed out by the moderator, I find it extremely regrettable or, should I say, disappointing. I say Miyazawa should stick with his own tune, no matter what. Whether the circumstances of his appointment as the finance minister would allow him to do so is not entirely clear, but I still say he should stick to his own view.

When I say he should stick to his own view, essentially I am talking about his approach to the handling of fiscal reconstruction--should he rush with it, or should he put it off? Even if it takes putting it off, at this particular point in time he should try to stimulate the business at all cost so that Japan could fulfill its responsibility as a member of the international community. Unless we go in this direction, I have the feeling that the consequences are likely to be quite grave, and this is why I would like to see Mr Miyazawa stand firm.

In the final analysis, Nakasone, too, would like to follow this course of action, but having talked so much about fiscal reconstruction in the past, he cannot change his coat so easily. For this reason he wants Miyazawa to do it on his behalf--my hunch tells me this may not be too far from the truth.

C: That is what I am talking about. In some way, these two men--Nakasone and Miyazawa--seem to have started off on the understanding of scratching each other's back; in other ways, they seem to be looking daggers at each other under mutual distrust and wariness. The game is yet to be played out. Their relationship is neither a complete reconciliation nor a complete surrender. As such, politically speaking, their matchup is a delicately balanced work of art made out of compromise and confrontation.

As Mr D wished earlier, I think this whole question is still pending. Maybe his emphasis has changed somewhat, but it cannot be concluded that he, Miyazawa, has changed his coat. Perhaps it is more likely that Miyazawa, convinced that internal and external conditions will from here on work out in his favor, simply decided to quietly observe the situation at least for the rest of this summer.

To be honest, I am somewhat different from Mr B in that of late I am calling Nakasone as a great prime minister with few parallels in history. (laughter) Anyway, this prime minister called in his cabinet members one by one and gave them words of exhortation individually--exhortations by the great prime minister. He kind of likes to do these ceremonial things.

On that occasion, Miyazawa was the first to be called in. At a press conference held upon his return from the prime minister's office, Miyazawa stated: "I told the prime minister that, inasmuch as he was kind enough to appoint me as finance minister, I wished he would leave the fiscal and economic policies

up to me for a while at least." When this was reported to him by one of his lookouts, Nakasone reportedly remarked, "Did he indeed say something like that to me?--I don't quite remember." I believe this episode exemplifies the relationship between these two men.

Miyazawa sees this situation moving in his favor. I do not believe he has already made up his mind about the question of tax cut and tax increase. As I said at the beginning, for Miyazawa a tax increase is not something he will not do but rather something he won't be able to do in the end. There are many stages which a tax increase proposal must pass through: The government Taxation System Council is one and the party's Taxation Council is another; the government must make up its own mind about it, and there is the deliberation in the Diet--if the proposal ever reaches there. Miyazawa believes that the proposal will not survive in the end. I do not think his view on this is any different now.

B: Mr C, you just said that Miyazawa sees the situation developing in his favor, but what exactly did you mean by that? Are you saying that the economy will turn for the worse?

C: In other words, the pressure will...

B: Will make things difficult--is this what you mean?

C: Yes.

B: Therefore the time will come when the ideologue Miyazawa's number will have to be called after all. This, as you say, will work in Miyazawa's favor.

C: Exactly. So, picking up the thread of our earlier discussion, it may very well be that Nakasone is inwardly prepared to make a cat's paw of Miyazawa in that event and then discard him if necessary.

A: All this may be a par for the course for politicians. Still I am somewhat chagrined because, if that is what is in store, there is little hope that the expression "a simultaneous and matching tax cut and tax increase is the basic policy" will be revised. In the case of Nakasone, with a straight face he rejected the idea of a large-scale indirect tax--granted he did this in the heat of the election campaign. On the other hand, it simply should not have happened for a man of Miyazawa's disposition to say something like "a simultaneous and matching tax cut and tax increase is the basic policy." Being such a clever man that he is, Miyazawa could have put it in a somewhat different way.

#### Problems Related to Simultaneous, Matching Tax Cut/Increase

B: Revising that statement alone will not do any good. A tax cut first followed by a tax increase 2-3 years later--this, I can go along with. Should they insist on simultaneity, the only thing to do is to drop both ideas--tax cut and tax increase.

A: To put it in more loftier terms, Mr Miyazawa, despite his own background of having been part of the Finance Ministry bureaucracy, is a man of caliber far beyond the class of the finance bureaucrats. By this I am talking about his very rich sense of worldliness.

When it comes to those currently serving in the Finance Ministry, I am amazed by their small-nation mentality. In other words, their thinking is motherland-centered--all they think about are their own country and their own ministry. This is the kind of organization the Finance Ministry is. Despite such strong internal and external pressures as we have today, demanding Japan to play an international role, those in the Finance Ministry are insisting that the first thing they must do is to put the fiscal administration in neat order, as if doing so is the answer to all other problems. This, I think, is the proof of their motherland-centered mentality.

Straightening out the fiscal administration is of course necessary, but there is no reason to rush--no harm in delaying it a little. It can be done gradually, and right now what is being demanded of us internally as well as externally ought to be given priority attention. At this moment, when the government officials need to have a little more of the big-nation mentality in the positive sense, those in the Finance Ministry are still operating with the small-nation mentality, putting their own country and own ministry ahead of everything else.

It is right there in this ministry where we now have a man of Mr Miyazawa's caliber--a man who has the big-nation mentality in its positive sense and also has a sharp sense of internationalism--in charge, and as long as he is already there, he should do no less than remolding those finance bureaucrats to some extent. In this context, at least, I tend to believe that there is a role for Miyazawa to play.

C: I wonder whether you, Mr A, might not have gone a little too far in depicting the relationship between Miyazawa and the finance bureaucrats as confrontational in nature. There is another factor: Right now, an internal conflict is brewing among the finance bureaucrats themselves. I believe a fair number within the Finance Ministry are now airing the view that the world does not belong just to those who are running the budget or the tax bureaus.

A: What do you mean specifically?

C: It is just that I somehow feel a more specific pattern will emerge as the struggle between the opposing sides progresses, but I am not sure.

B: Earlier it was pointed out how rich Miyazawa is in the international sensibility, but I believe the man is, in some sense, pax-Americana. Although we are still under the postwar system in which the strong presence of the United States as the boss is accepted, Miyazawa can be quite critical of the United States at times--he points out, for instance, that the United States ought to have a firmer grip on itself.

A: I did not mean to say that he will blindly follow every command of the United States.

B: I dare say that he has no inclination to help out the United States only to see Japan become the second-ranking international leader next to the United States.

D: Nevertheless, not only does he have a sharp antenna, I think his way of thinking is, at least among Japanese politicians, richly disposed toward internationalism as well.

Incidentally, when Mr C interviewed each of the three "new leaders" individually before the election, Mr Miyazawa made a statement expressing his desire to make use of the bureaucratic structure. He said that the bureaucratic structure is extremely fine in quality and that it would be a folly not to make use of it. I do not know whether at that time he was interested in becoming the finance minister or not. With regard to the power relationship between Finance Minister Miyazawa and the bureaucrats of the Finance Ministry, the moderator said that the former is a natural enemy to the latter, but I tend to question the validity of that view.

C: I, too, did not quite understand that part.

D: Since I do not understand the point very well, if you would kindly explain it a little, I am sure it will help clear the future outlook for me.

A: Essentially what I meant to say was this: The Finance Ministry is the largest model of the bureaucratic organizations. As to who holds the power in this ministry, it is those who have served in the budget bureau, inevitably. This has been an unchanging formula. The rotationary course from director of the minister's secretariat to director general of the budget bureau and then to the vice minister is still firmly in place, and this line has always constituted the ministry's mainstream. Accordingly, in viewing the ministry's personnel actions, one only needs to keep this established pattern in mind: Whoever becomes director of the minister's secretariat, he is destined to move up to the positions of director general of the budget bureau and then the vice minister in 2-3 years' time. This cycle has not changed at all over the years.

Mr C has depicted this established pattern as something of a dilemma that is driving the Finance Ministry into a dead end; he has also said something to the effect that there is an internal conflict brewing in the ministry as a result of the emergence of new forces from outside of the traditional mainstream. But at least as things stand now, Mr Yoshino, the incumbent director of the minister's secretariat, is bound to become director general of the budget bureau and then the vice minister. There is no question that, under the existing circumstances, the budget bureau will continue to make up the mainstream; just as certain is the introduction of a large-scale indirect tax being a desperate wish of those in the budget bureau.

In addition, the Finance Ministry is still unable to drop the slogan that calls for the clearing of all deficit bonds by fiscal 1990. Even though some in the ministry are inwardly aware of this slogan being a sheer dream of dreams and some are even saying so outright, the fact that the slogan cannot be dropped is a proof that the ministry's power structure consisting of the budget-bureau mainstream is still in place intact.

Not to the ministry as a whole but to those of the mainstream, Mr Miyazawa--though a senior alumnus to them--is a presence who is not only aggravating but also simply untrustworthy. This feeling was reflected when a key official of the ministry--a top class official--dismissed one of Miyazawa's ideas as something which might be expected of the division-chief-level officials of the ministry--the idea of handling the redemption of matured bonds wholly by means of refunding bonds, which Miyazawa floated when he was chairman of the party's executive council and which has come up in our discussion today.

This shows the extent of feelings against Miyazawa among the officials of the Finance Ministry. This is why I described him as the ministry's natural enemy, but more specifically he is a natural enemy to those bureaucrats who form the mainstream of the ministry.

Is the Framework of the Fiscal Reconstruction In for a Change?

C: What I have been saying is not that different from what you have just said. Nevertheless, it is also true that a fair number of today's younger officials have come out arguing that this kind of a "Budget Bureau runs Japan" perspective simply would not do. It is in this atmosphere that we are now beginning to see more interchange of personnel among different components of the ministry--the budget and tax bureaus on the one hand and all the other components on the other.

In view of these new developments, the situation in the Finance Ministry is not necessarily a squaring match between right and left. Take the Miyazawa's side, for example: When he said that the bureaucrats are an outstanding bunch, on the one hand he was throwing a preelection broadside against Nakasone's reliance on brain trust for running the government, and on the other hand he was expressing self-confidence in his ability as a politician to get a full mileage out of the bureaucrats through skillful handling. Now that he is sitting at the Finance Ministry, the house of the most bureaucratic bureaucrats, it remains to be seen as to how well he handles them.

Those are the things I had in mind when I made the earlier remarks. In short, I do not believe that the so-called natural-enemy relationship between Miyazawa and the finance bureaucrats will continue to prevail as a permanent thing. This is all I am saying.

B: That sounds reasonable.

D: If so, looking ahead, which side do you think will have the initiative-- Miyazawa or the bureaucrats?

B: A case of tug-of-war, perhaps? If, as Mr C is saying, the situation gradually turns in Miyazawa's favor, the finance bureaucrats are likely to get on the bandwagon.

C: By the way, about the small-country mentality of the Finance Ministry's mainstream which Mr A was referring to, I guess it is something firmly entrenched. Those people are the believers of finance for finance's sake, after all.

A: They are indeed that; also, policywise, their highest priority is on fiscal reconstruction. Everything else can wait as far as they are concerned.

B: Among the finance bureaucrats, there are some exceptions as pointed out by Mr C, but by and large they are used to being thrown into tizzy by politicians, especially in regard to budget-related initiatives. Be that as it may, Miyazawa's suggestion concerning the refunding bond falls into the caliber of ideas which the division-chief-level bureaucrats may come up with.

What really bothers the bureaucrats is when politicians tell them things such as "Give up both tax-cut and tax-increase schemes," "Change the policy and cut taxes first," "Consider cutting taxes on condition that taxes are to be increased after 2 years," and "The goal of completing fiscal reconstruction by fiscal 1990 ought to be changed." As for the last item, it is indispensable that the goal be met as planned. It cannot be changed unless the nominal growth rate rises. Once inflation subsides, the whole scheme will fall apart. The suggestion that it be changed must therefore come as a shock to the bureaucrats. When it comes to the suggestion of issuing refunding bonds, the bureaucrats must find it truly annoying--they probably take it as if someone is trying to dip into their own pockets.

C: Although it is hard to predict, when Nakasone's term of office is given a 1-year extension and when the time comes for a supplementary budget in the fall, it may very well be that Nakasone, riding on the crest of his power, would change things around with no compunctions. How likely do you think the possibility is for a policy shift--delaying the basic timetable of fiscal reconstruction, for example?

B: Conspicuous transformation? Such a change might be possible if you Mr C so advises Nakasone.

A: Mr Miyazawa is saying that there is no need to change the target year as now set for fiscal 1990, nor should it be changed. Difficult though the target might be, the reason for having it set is to use it as an imperial standard to force reductions in the government spending. It makes sense.

C: Another symbol like the 1-percent ceiling for defense spendings?



A: After all the finance bureaucrats themselves are calling it a dream of dreams.

C: So why not leave it at that for the time being?

D: Come to think of it, ever since the days of Prime Minister Ikeda, Miyazawa has been a believer in the economic growth policy, basically. As such, he is more pleasing to the MITI people than to the finance bureaucrats. He has this disposition policywise. Knowing this, the business people are screaming about the unbearableness of the strong yen and noisily calling for actions to stimulate domestic demand. I believe this voice will become considerably louder by this fall; also, external pressures will increase even more.

In that event, Miyazawa, the torchbearer of the Ikeda legacy, may find the environment more conducive to the unfolding of the kind of policies that would be more in line with his disposition.

Such being the case, beginning this fall, it will be tail wind for Miyazawa and head wind for Nakasone. When that happens, Nakasone being what he is-- a man with unquestionably superb qualities of a politician...

C: A weathercock.

D: Right. So, he may very well make a switch so as to accommodate internal and external demands. Such a shift could come as early as this fall, especially if it turns out definite that he will be securely in power for another year. What do you think?

A: I believe this happened after Miyazawa had accepted the finance portfolio: In talking about his appointment, he likened it to "a chestnut in fire"--his exact expression. The question is, what specific aspect of being the finance minister did he mean by that expression? I thought he was referring to the prospect of being made the front man for the risky job of raising taxes, but it does not look that way now that I have heard your views.

From Nakasone's standpoint, Miyazawa is a man who freely and abundantly spoke his pieces in the past. Perhaps Nakasone's thought was: "You have said plenty. Now I will make you the finance minister so you can try and see yourself whether those things can be done." Was Miyazawa made to risk his own neck for that reason, or did Nakasone simply want to thrust the most nasty business of tax matters onto Miyazawa? As I said, I thought Miyazawa was referring to the tax-increase matter when he used the expression "a chestnut in fire." Is this interpretation off the mark?

B: I think it is reasonable.

A: By the way, Mr Shoyo Ito, the author of the book "History of the LDP's Warring Years," is he one of the cheering parties for Miyazawa?

C: I believe he is neutral.

A: The grapevine has it that Mr Shoyo Ito has been saying some words of encouragement: Specifically, he is telling Miyazawa not to look at his situation as a case of picking up chestnuts in fire but as an opportunity to find a new life out of death. As to what Miyazawa ought to do, he is saying that putting forth countercyclical measures in an aggressive and daring manner would suffice.

The same grapevine also has it that Mr Ito has been advising Miyazawa along the following lines: Come up with your own idea that runs counter to Nakasone's and do the best you can with it; even if you fail, so what of it!? As long as you pursue your goal aggressively and boldly, the business world and the public will support you--not only that, they will come around to becoming your cheering party.

Picking up chestnuts in fire, finding a new life out of death--all this sounds so simple but, as Mr C has been saying, for a politician things just do not work out by such simplistic formulas; rather, zigzagging and trial and error are more a rule than exceptions. Also, if there is anything to these expressions, "chestnuts in fire" and "life out of death," one might ask which is better or takes more strength--doing the former or trying the latter?

Can Miyazawa Gain a Business-World Cheering Corps?

C: It is impossible to say at this stage. Politics is not that cut and dry--it is neither picking up chestnuts in fire nor finding a life out of death. As it was just pointed out, meandering is the norm and the victory or defeat is decided somewhere along this winding path. It is in this context that I have been saying that Miyazawa's role is the most interesting point to watch with regard to this new cabinet. How it will all come out, I cannot tell.

D: I would like to get your views regarding Prime Minister Nakasone's source of political funds. I think he is in for increasing pressure from the financial world, and I have the feeling that whether or not he will give in to this pressure depends to a considerable degree on the state of his pocket-book. It makes me wonder what kind of money pipeline he has. Since the days of the Kono faction, those in this group have not had much of connections with the mainstream of the financial world; even now the picture does not seem any different. There is Mr Doko, but he is a nonentity--or pretty close to it--in terms of being a money pipeline. I am curious about Nakasone's source of funds because I believe it has the bearing on the extent to which he must pay close attention to the voice of the business/financial world.

C: In today's Japan, the old practice--and all the nuances connected with it--of each political faction maintaining its own, different source of funds has diminished to a large extent. Now, under the new system that has evolved, it works this way: From season to season, as they say, when the person then holding the highest power gives the word regarding funds, his wish is accommodated suitably. This is one source of Nakasone's funds.

Then there is the fund-raising operation of Nakasone's mainstream. There used to be a lot said about alleged stock manipulations by Mr Ikeda, but in the case of Nakasone's mainstream, some say that the "Min Katsu" [utilization of the private sector] approach is the key to their fund raising. To be more specific, unlike the old Kono faction that was hard put for funds, Nakasone has matrimonial ties with the Kajima clan and Noboru Goto of Tokyu Corporation is a close friend of his from their youth days. Nakasone has no shortage of such connections. "Mitchi" Watanabe [Michio Watanabe], former minister of international trade and industry, is another such connection. I have been calling Mr Nakasone as an uncanny prime minister for good reasons. His recent personnel actions were a case in point--for instance, the way he so unceremoniously dismissed Mr Mizuka and grabbed Mr Mutsuki Kato instead, and the manner of his handling the case of the party's Vice President Nikaido. Of course these are matters of politics, but the point is, I do not believe Mr Nakasone is susceptible to any undue attempt to influence him in such areas--that is, as far as power relations are concerned.

B: That is why he may be considered a great man, in some respect. In this regard, don't you think Miyaza, too, has a similar quality? Lately I have been traveling to Gifu Prefecture quite often. One day before the election, I got off at Hanushima in that prefecture and there was a large crowd at the station. Then I saw Mr Takeo Fukuda getting off the same Shinkansen train which I took. He had brought Ms Chikage Ogi with him as part of his entourage. As soon as he got off the train, he went into enthusiastic hand-shaking with those of his supporters' association present there. And he looked so genuinely happy shaking those hands.

This man Fukuda has always been one of the down-to-earth kind. If one compares Nakasone and Fukuda, the latter comes out on top. Fukuda is a born leader. He is down-to-earth, has the old boss-like qualities and his enthusiasm is natural. Nakasone cannot act this way, even if he tried.

All this means that it takes certain qualities for a man to come out on top. Take "Kakuei-san" [Kakuei Tanaka], for example: whether he is in jail or paralytic, it does not matter--he still comes out on top. Mr Miyazawa has never been a top winner. I guess it takes more than functionalism for a man to be a top winner in an election.

D: Takes the "naniwa-bushi" style?

B: Exactly, the naniwa-bushi is it.

C: I am absolutely in favor of that.

B: In this regard, there is a fair amount of similarity between Nakasone and Miyazawa.

C: I have always wondered why political reporters insist on pointing out in their reporting which politician was the top winner in what electoral district and which one was the runner-up. I think this is truly absurd. I say it is absurd only in the context of what Mr B was talking about. Just

because a man was the top winner in his own district, does that make him a great national leader? Any notion of drawing an analogy between the two strikes me as a downright folly.

B: I have had several roundtable discussions with Mr Fukuda--perhaps Mr A was in on some of them, too. These sessions are usually arranged by a strange-looking, fixer-like man who is a publisher of a magazine. Even on such occasions, if Mr Fukuda were a reluctant participant merely going through the motion, he showed no signs of it. On the contrary, he would greet others enthusiastically by slapping their shoulders and saying things like "Why hello, how are things with you?"

C: That's him, all right.

B: That's the way he is. He is a topnotch--positively. On the other hand, men like Nakasone and Miyazawa belong to another ilk.

C: They are stylists, that's why.

A: Mr C has said that Mr Miyazawa seems to be of the view, deep down, that a tax increase cannot be done. Although a lot is going on right now between Miyazawa and the finance bureaucrats, the matter is still entirely pending.

Mr B's points were: If a tax increase is doomed, then a tax cut, too, is a dead issue; so, this was what Miyazawa actually meant when he stated that the basic line was to go forward with simultaneous and matching tax cut and tax increase; Miyazawa was not suggesting that the two be undertaken together--he was saying nothing can be done unless the two issues are dealt with at the same time; thus, if one goes the other goes as well--this is the emerging problem. Among various views aired today, I find these points of Mr B's quite impressive.

At any rate, Mr Miyazawa is ready to "pull the chestnut from the fire"--he has said as much in talking about his frame of mind. Among Miyazawa's cheering party, some are urging him on to "find a new life out of death." Be it a case of pulling chestnuts from the fire or a case of finding life out of death, either way Mr Miyazawa's political mettle will be in for a test. This coming fall will probably be the crucial time for Mr Miyazawa. At the same time, all this will constitute a point of extreme interest in closely monitoring the future direction of fiscal and economic management in Japan.

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POLITICAL AND SOCIOLOGICAL

BACKGROUND TO NLC'S RETURN TO LDP DESCRIBED

Tokyo SENTAKU in Japanese Sep 86 pp 58-59

[Text] Yohei Kono Who Has Closed the Books on His Life of "Endurance"

The smaller the household, the fiercer the discord between its members; a squabble that ends without getting out of control in a large household often becomes a deadlock in a small household. By the same token, things go rather well in a large, extended family but troubles abound in a nuclear family. It is this axiom that has been vividly demonstrated in the course of events leading to the return of the New Liberal Club [NLC] to the fold of LDP.

The NLC's 10-year history was literally a chronicle of intraparty strife. On the evening of 11 August, to iron out final details of the NLC's return to the LDP, NLC representative Yohei Kono and LDP Secretary General Noboru Takeshita held a secret meeting at Keio Plaza Hotel, Shinjuku, Tokyo. During the meeting the following exchange--somewhat jestful--took place:

Takeshita: How have things been with you these past 10 years, Mr Kono?

Kono: I have simply learned how to endure and endure some more.

Takeshita: The same holds true for me, too.

Kono: Shall we say you are the grand master (in the art of endurance) and I a certified graduate?!

Incidentally, Takeshita is well known for his patience--no one has ever seen him angry. He endured as usual even when Kakuei Tanaka called him "still only a floor mopper." The only thing is, in Takeshita's case he had a broad layer of supporters backing him and, as a result, his endurance at a given stage led him to the next phase of his career evolution. By contrast, Kono in his small political household was forced into a kind of endurance that was nearly isolated and without promise.

Kono's bad luck and narrow-mindedness did not help the situation, either. If at the onset he had taken advantage of the favorable tide and managed to form a mid-sized party of 20-30 persons, the NLC's fate would have been different. In that event, even the internal strife, perhaps mitigated to a degree by the

size and strength of the party as a whole, would not have grown as much as it did. But more than anything else, his biggest misfortune was that he had few truly trustworthy followers around him.

Even Takeo Nishioka (NLC's first secretary general) and Secretary General Toshio Yamaguchi--the two men widely regarded as Kono's right and left arms--turned out to be the culprits who in the end pulled the rug out from under Kono's feet. All three of them--Nishioka, Yamaguchi, and Kono--are second-generation Diet members, but they lacked the placidity usually characteristic of the second generation. Their self-indulgence, resulting from the lack of appreciation of the pains attendant to those on the lower rungs of the ladder, got the better of them; as a result, by and by they have fallen victims to the war of attrition of the nerves.

Nishioka, a headstrong man, fastidious to a fault, brooded while Kono refused to budge in their confrontation over political lines (Kono's "two-conservative party theory" versus Nishioka's argument for "another party rooted in the LDP")--a confrontation that was not entirely beyond mend. Nevertheless, there was a saving grace in his case in that his clashes with Kono were mainly of an ideological nature. Even when he raised the flag of rebellion against Kono, he was indecisive. Long after the die was cast, he was often heard complaining, "The mass media did me in!" It indicated his anger that he was prematurely forced out of the party before he had made the final decision to leave it owing to the big splash made by the press. Nishioka's revolt may also be viewed as his own way of putting an end to his involvement with the new party, which had been a case of incomplete combustion all along. Kono, on his part, fully aware of all this, was resigned to the inevitability of the rupture in his relations with Nishioka.

On the other hand, Kono's discord with Yamaguchi was inherently much more troublesome in nature. A man of small stature but unusually ambitious, Yamaguchi would not hesitate to use any means to get what he wants once he makes up his mind. Soon after the formation of the NLC, he began maneuvering to win the majority over to his side by spreading the words that "The party leader does not necessarily have to be Kono; I can handle it just as well." This kind of scheming within a miniparty like the NLC was like the LDP's interfactional strife transformed into a fight between individuals--it became uncontrollable. It led to a worsening emotional confrontation.

Nevertheless, the NLC came into being with a strong image of being "the Kono Party" to begin with. What troubled Yamaguchi was the fact that NLC without Kono was simply unthinkable. With this realization, Yamaguchi quietly began regrouping. Accepting the unavoidability of keeping Kono as the titular head, Yamaguchi wanted to transform NLC into a de-facto "Yamaguchi Party" and then, at an opportune moment, he hoped to sell out to the LDP for the highest price.

Thanks to Yamaguchi's uncanny cleverness and gall, his scheme made considerable headway. Labeling Kono--a man of honorable poverty and no compromise by inclination--as an "incompetent politician," Yamaguchi made his money power and willingness to compromise as a selling point in his campaign to proselytize NLC members holding Diet seats as well as NLC's secretariat--with

some success. Kono became isolated. Kono's friends within and outside the NLC and sensible members of the LDP urged Kono to "break off with Yamaguchi," pointing out that "failure to act promptly would result in dire consequences." But no bright ideas emerged. Kono's endurance fast approached the limits with each passing day.

Kono's narrowmindedness was a contributing factor to his inability to embrace and nurture Nishioka and Yamaguchi into his confidants. On the other hand, even if Kono had such an embracing capacity, chances are the apparent "personality conflict" might very well have made it impossible for him to keep these two men in his fold. For Kono, it was simply a case of an ill-fated encounter--there is no other way to describe it.

Growth was out of question for a strife-ridden minipolitical party. Kono seriously began to consider the idea of returning to the LDP's fold in December 1983 following the LDP's election defeat and subsequent formation of a coalition with NLC. It was, in his judgment, the only available escape hatch--no matter how he looked at the situation.

On the question of returning to the LDP, there was no disagreement between Kono and Yamaguchi, although their ulterior aims were different. Yamaguchi was an advocate of selling out at the highest price; with this in mind, he even considered the idea of rejoining LDP shortly before the double elections of both houses of the Diet. On the other hand, Kono quietly resolved not to let Yamaguchi have his way in the settling of the question of dissolving the NLC and returning to the LDP. Yamaguchi reportedly made the following proposition: "Let us be the Kono faction after rejoining the LDP, but how about passing the factional leadership to me after 3 years?" But Kono had no such intention--even if they were to return to the LDP together, Kono intended to part ways with Yamaguchi afterward.

An opportunity presented itself for Kono--it came in the form of the LDP's overwhelming victory in the elections. This turn of events took the air out of Yamaguchi's "high price" approach, but Kono saw in the very development, which depreciated to NLC's value to its lowest, a favorable opportunity to act. It could be that Kono, who had on occasion been criticized for being overly appearance-minded, purposely chose to endure the humiliation of returning to the LDP under the most unseemly and unwelcome circumstances.

About 10 days after the double elections Kono began his move under extreme secrecy. He warned those around him to be discreet because "any leak to the press would kill the whole thing." He was mindful of possible adverse reaction from within the LDP, but his bigger concern was about the likely interference by the Yamaguchi group. In the end, it was not until after an agreement had been worked out between Kono and Prime Minister Nakasone that Yamaguchi learned about it.

By striking this last-minute counterblow against his rivals, Kono seems to have finally closed the books on all the endurance he had shown over the years. In doing so, he succeeded in staging a scene in which he played a role most becoming of the party leader--more so than any other times throughout his 10 years with the NLC.

Come 15 January next year, Kono will be 50 years old. He was first elected to the Diet at age 30, became the leader of NLC at 39, and rejoined the LDP when he was 49. He has made major moves of his political life at just about 10-year intervals. The next 10 years, however, are likely to be the most difficult interval for him.

The question now is, will the move from a small household [NLC] to a large family [LDP] enhance the position of the Kono type or will it boost the fortune of the Yamaguchi type? For these two men who are poles apart in character and style, a new round of fight has just begun--this time, on a different stage.

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## POLITICAL AND SOCIOLOGICAL

### CABINET SECRETARIAT REORGANIZED

Tokyo SENTAKU in Japanese Aug 86 pp 126-129

[Text] On 1 July, when the Japanese islands were wrapped in the fever of concurrent upper and lower house elections, the cabinet secretariat, which is directly connected to the prime minister, quietly started to reorganize. Japan's administrative structure was said to have become "all ministries and agencies, and no cabinet," so, as a result of the report by the Ad Hoc Council on Promoting Administrative Reform, which advocated stronger cabinet involvement, the government carried out the "largest scale reorganization of the cabinet secretariat in the 40 years since the war" (Chief Cabinet Secretary Gotoda).

However, since the topic itself was rather simple, the people did not notice; the government was consciously "performing" quietly, so this action was veiled.

Prime Minister Nakasone declared that, "the style of politics where documents and signatures are passed around from section chief to bureau head, from bureau head to vice minister, and from vice minister to minister is outdated. I (Nakasone) give instructions to the vice ministers and bureau heads of the various ministries and agencies by phoning them directly. I am promoting speedy politics." For Prime Minister Nakasone, who aims to be an American-style presidential prime minister, this cabinet reshuffle is literally a strategy for making the strengthened prime minister's residence into a White House.

With a great victory of 304 Diet seats, centralization of police, defense, security, and overseas information has begun, as well as concentration of these in the prime minister's residence, and the "Nakasone White House" is becoming strong in the three areas of structure, personnel, and information.

Making the prime minister's residence into a "White House" is likely to reduce the authority of the Ministry of Finance. From what we can see of the reorganization of personnel in the residence, it seems that the defiance of the old Ministry of Home Affairs, particularly of the secretariat of Police, vis-a-vis the Ministry of Finance has just surfaced. In any case, we see the old Ministry of Home Affairs' "scrap" strategy of Nakasone and Gotoda toward the Ministry of Finance when they say, "the economic secretariat has little knowledge of administration of state affairs."

Prime Minister Nakasone actually gives the Ministry of Finance very low marks. His view of the Finance Ministry is that "the Finance Ministry secretariat cannot think of anything unless it is peeking into its wallet. The idea of governing the state is too confining, and has no 'dynamism.' Those members of the government tax adjustment committee who come from the Finance Ministry are extremely conservative and inflexible. Several people from the private sector have landed on a runaway horse."

#### The Scope of Defense Spreads to All the Ministries and Agencies

Although people seem to understand what the "cabinet secretariat" is, they don't always, so, before getting into the issue of reorganization of the secretariat, let's briefly touch on the cabinet secretariat.

The prime minister has "two faces." One is that of the head of the cabinet that he sets up as minister of the state. The cabinet secretariat is the administrative authority for that body. The Cabinet Act states that, "the cabinet secretariat organizes cabinet matters and coordinates all other important matters concerning cabinet affairs and meetings. The cabinet secretariat also takes charge of gathering information on important cabinet policies, and carries out important coordination to maintain unity of the various administrative agencies on policies." (Article 12)

In short, the work of the cabinet secretariat is to coordinate the various ministries and agencies, and to collect information. Because of drastic social changes, there is little administrative work a given ministry or agency can do by itself, as it used to. The idea of something extending over several ministries or agencies is strengthening, and coordinated administration is becoming very important. The person responsible for this in the cabinet secretariat is the chief cabinet secretary, and his deputies for administrative business affairs assist him.

It is not widely known that the prime minister, as the "chief minister" of the Prime Minister's Office, which is another administrative office, is in charge of administrative matters, just as are ministers of other ministries and agencies. In addition to administration of ceremonies, pensions, and statistics, the prime minister is in charge of matters that are not under the jurisdiction of other ministries and agencies.

The Prime Minister's Office is divided into the minister's office and an extra-ministerial bureau, which exercise control over these matters. In addition to the offices the prime minister "heads," such as the Defense Agency, Economic Planning Agency, Science and Technology Agency, National Land Agency, and Environment Agency, there are administrative committees such as the Imperial Household Agency, the National Public Safety Commission, and the Fair Trade Commission.

There is a "secretariat" in the minister's office, but this secretariat is in charge of the ceremonies and pensions mentioned earlier. Thus the "cabinet secretariat" and the "secretariat" in the minister's office are structurally separate organizations. However, almost all of the staff serves on both

secretariats. For example, Furukawa Teiji serves as chief councilor in the cabinet secretariat, as well as director-general of general affairs in the prime minister's office; secretary Ogane serves as director of personnel in the prime minister's office.

The chief cabinet secretary, who is the person of responsibility in the cabinet secretariat, has tremendous influence politically, as well as administratively.

The chief cabinet secretary's office is located on the second floor of the East section of the prime minister's residence. After passing through the secretary's office and the small reception room, one enters the chief secretary's office. In the back of his office, on the left, is an executive desk, in which there are two safes. Usually there is close to Y10 million in cash in the safes, and there are times when there is more than Y50 million.

These are cabinet secretariat coordination funds, commonly called secret funds. If the chief cabinet secretary phones the secretary (the director of the accounting section of the prime minister's office) and says, "please give me a little," he can get it that day.

These secret funds are political activity funds which can be used without obtaining vouchers, and are sacred funds which even the Board of Audit cannot check. Often dietmembers visit the prime minister's residence to pay him a call before they travel overseas, and when they leave, they stop by the chief cabinet secretary's office to receive a farewell gift. The amounts vary from Y500,000 to more than Y5 million, and there are times, such as when a dietmember is wearing a thin summer suit, that one can see a white envelope bulging out of the pocket of a dietmember leaving the prime minister's residence. It is said that this secret fund is also used for Diet funds, including for the opposition party at the time of deliberations on important bills, and for Akasaka restaurant politics, and is said to amount to Y2 billion per year. This comes out to more than Y7 million per work day.

This backs up the power of the chief cabinet secretary.

Even looking at the fact that "a prime minister's authority extends indirectly even to a private airline company's choice of airplane" (the Lockheed scandal decision), it can be said that the chief cabinet secretary oversees a large area administratively, and that, politically, this extends to all the ministries and agencies.

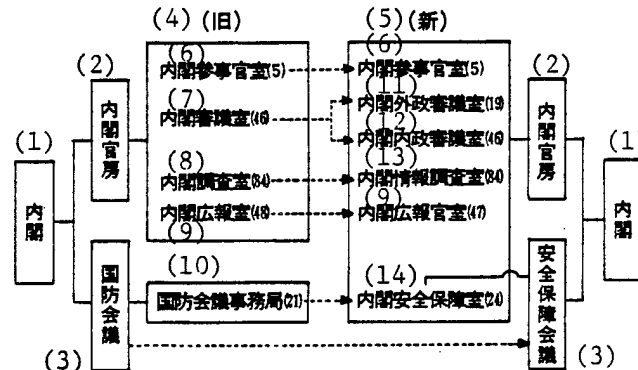
Of this broad scope of responsibilities, we have tried here to focus on the reorganized structure.

In Any Case, Foreign Policy Is Under the Direct Control of the Prime Minister, Isn't It?

So this is the cabinet secretariat reorganization, and, as can be seen in the following chart, the cabinet secretariat which had been made up of four offices, will now be comprised of six offices. From the chart it appears

that this was a simple reorganization, or change in titles, but that is not the case.

The New Structure of the Reorganized Cabinet Secretariat  
(the numbers in parentheses indicate the number of personnel)



Key:

- |                                    |   |
|------------------------------------|---|
| 1. Cabinet                         | 10. National defense council secretariat            |
| 2. Cabinet secretariat             | 11. Cabinet councilor's office for foreign affairs  |
| 3. National defense council        | 12. Cabinet councilor's office for domestic affairs |
| 4. (Old)                           | 13. Cabinet information research office             |
| 5. (New)                           | 14. Cabinet security office                         |
| 6. Cabinet counselors' office      |   |
| 7. Cabinet councilors' office      |   |
| 8. Cabinet research office         |   |
| 9. Cabinet public relations office |   |

The revision that is considered most important is that of the establishment of a cabinet security office. In the past, the secretariat of the National Defense Council was established under the law which set up the Defense Agency: It dealt only with defense issues, and was not part of the cabinet secretariat.

In contrast, this time, a security council was set up under the independent security council establishment law. The security office forms part of the cabinet secretariat, while also acting as the secretariat of the security council. In addition, the security office deals not only with defense issues, but is also responsible for handling crises related to the lives of citizens, such as terrorism and hijackings, large fires, international incidents such as MIG 25 incidents and the shooting down of the KAL plane, and economic difficulties such as the oil crisis. At present this is completely wrapped up in a veil, but in the case of an emergency, the security council will also be in charge of areas that are not clearly under the jurisdiction of other ministries or agencies (classification 3 of the so-called emergency legislation research), such as "evacuation and encouragement of residents in an emergency," and "the handling of prisoners."

Since it is clear that this is not a simple reorganization of the national defense council secretariat, it could be considered to be the establishment of a new organization under the direct control of the prime minister.

The cabinet councilors' office for foreign affairs is what its name says, and since it is the so-called face of this cabinet secretariat reorganization chart, it seems to be well known.

In the case of negotiations with other countries on overseas economic issues such as trade friction and economic aid, domestic coordination will be necessary. So far there have been frequent cases in which Japan has ultimately made large concessions to other countries in the form of expanded quotas for beef and oranges, lowered tariffs for timber and tobacco, and voluntary restraints on the export of automobiles to the United States, due to the fact that it took too long to resolve domestic conflicts between the Ministry of Foreign Affairs and the Ministries of Agriculture, Industry, and Finance.

The establishment of the councilors' office for foreign affairs is an attempt to control this from the cabinet level, and handle such matters speedily. Diplomatic negotiations will be handled primarily by the Ministry of Foreign Affairs, and domestic coordination on diplomacy will be carried out by the councilors' office for foreign affairs. While it would not be appropriate to call this a "duplication of diplomacy," we cannot overlook the fact that, structurally, the cabinet secretariat has a start toward affecting diplomacy.

The "Information Research Office" Aims To Be a Full-Scale Information Organization

There is another inconspicuous change which has not really been noticed.

The cabinet research office, also known as JCIA, became the cabinet information research office. None of the personnel changed, so there is a tendency to think that this simply was a name change. However, by a revision of the cabinet order, the purpose of this office was expanded to include "analysis" as well as its former purpose of "collecting information and making surveys."

Taniguchi (Shusei), director of the cabinet information research office, says, "We have carried out analysis in the past. This was merely a change in the cabinet order to reflect the present situation." However, it is clear that purposely changing the cabinet order is a step toward creating a full-scale information organization.

This surfaced in an episode concerning the English title of the cabinet information research office. Originally the strongest proposal was that for calling it the Cabinet Intelligence Office (CIO). This followed the example of the U.S. Central Intelligence Agency (CIA) and South Korea's KCIA. However, it was thought that instead of simply meaning collection of information, the word "Intelligence" tended to give the impression of activities based on secret information and collection of information and strategic activities by spies, so, in an effort to minimize excitement, they settled on the name "Cabinet Information Research Office (CIRO)."

Judging from the present state of the cabinet research office, "Information" would be proper. However, we would not be digging too deep if we saw their attempt to make it "Intelligence" as a suggestion of the future direction.

This is not simply the restructuring of an organization. Prime Minister Nakasone is secretly advancing his efforts to make his residence a White House by gathering and controlling information.

The afternoon of 17 July, an unprecedented cabinet meeting was held in the large guest room of the prime minister's residence. This was the first information conveyance meeting. It was attended by only seven people, namely: Director of the Cabinet Information Research Office Taniguchi, Director of the Cabinet Security Office Sasa, Head of the National Police Agency's Security Bureau Mishima, Deputy Director of the Public Security Investigation Agency Tamura, Director of the Defense Agency's Bureau of Defense Policy Nishihiro, Acting Director of the Foreign Ministry's Information and Research Bureau Onodera, and the chairman of the meeting, Deputy Chief Cabinet Secretary Fujimori.

To lessen the tone of secrecy at this first meeting, the press corps was allowed to photograph the beginning of the meeting, but this will be prohibited hereafter, and the content of the meetings will not be made public. Furthermore, an agreement was made that, "at the meetings, minutes will not be taken and attendees will refrain from taking notes. Proxies will not be allowed."

The purpose of this meeting is to suck into the prime minister's residence anything that bears the name of information, such as police information, security information, defense information, and information from overseas, and to exert direct control over that information. The goal is to increase the volume of information gathered in the prime minister's office, and to improve its quality and the speed with which it is obtained by having the various ministries and agencies concerned with information compete to report information individually and at all times, not just at these meetings.

The prime minister has also proposed that he have lunch with the six directors of the cabinet secretariat offices on the third Friday of every month, and this is quickly moving toward implementation.

The prime minister presently has lunch regularly with the government/opposition party communication council on Mondays, and with the government/opposition party leaders group on Wednesdays, so it could be said that having lunch regularly with six office directors of the bureau chief level is preferential treatment.

Trying to obtain information directly by creating competition could be called a Nakasone-style information policy.

Making the prime minister's residence into a White House leads to a relative drop in the footing of the various ministries and agencies. It was because of this that the Foreign Ministry strongly opposed the reorganization of the

cabinet secretariat up to the time it was carried out saying, "the establishment of a councilor's office for foreign affairs will mean that the prime minister's residence will have a direct hand in foreign policy, and we cannot allow a double foreign policy."

The Ministry of Finance showed strong resistance in terms of personnel saying, "in the future, the prime minister's residence might even try to grasp the right to compile the budget, as is the case in the United States."

The personnel structure of the new organization was studied starting the end of May, but the Finance Ministry waited on appointments from the vice-ministerial level on down from the beginning of June. The Finance Ministry quickly brought together those personnel who had entered the ministry in 1953, 1954, or 1955, and unofficially decided on Matoba Junzo (1957, Ministry of Finance), who had been director of the cabinet councilors' office up to that point, to be director of the cabinet councilors' office for domestic affairs. It leaked this to the press.

The Ministry of Foreign Affairs had originally planned on having someone who had entered in 1953 or 1954, but in order to have a balance, it appointed Kunihiro (Dogen) (1955) as director of the cabinet councilor's office for foreign affairs, and prevented the new organization from becoming too serious.

Eventually it was decided that Sasa (Junko) (1954) would serve as director of the cabinet security office, Taniguchi (Shusei) (1954) as director of the cabinet information research office, and Miyawaki (Raikai) (1956) as head of public relations for the cabinet. This was somewhat smaller than the intent Prime Minister Nakasone had originally announced of "lining up vice-ministerial level aces."

However, we should note that, of the six cabinet secretariat office directors, including Chief Cabinet Secretary Furukawa Teijiro (from the Ministry of Health and Welfare) of the cabinet counselors' office, all but two (Kunihiro and Matoba) are from the old Ministry of Home Affairs, and three of them are police officials.

In the beginning, the name of Matsuda (Keibun), a science counselor for the Ministry of Foreign Affairs, was mentioned as a candidate for director of the cabinet councilor's office for foreign affairs, but he was originally from the Ministry of Self-Rule, and was dropped on the basis of Chief Cabinet Secretary Gotoda's judgment that "he would be too flashy, so let's drop him."

The reorganized cabinet secretariat started on 1 July. That was a day when the cabinet was in session.

This was during the election, and the five office directors could not go around making greetings, so they stood at the entrance to the prime minister's residence, and individually greeted the bureaucrats that came in.

Two bureaucrats, after shaking hands with them, went upstairs to the meeting room muttering, "What's this? Policemen on parade?"

Tightening up and loosening up on personnel was "Gotoda-style personnel."

Is the Main Purpose To Weaken the Ministry of Finance?

Even from here we can see the future strategy of the prime minister's residence in its goal to become a White House.

Last year was exactly 100 years since the cabinet system was set up. The United States has become accustomed to the fact that the White House took the right to compile the budget from the Treasury Department. In 1939, the military authorities tried to incorporate the function of the Finance Ministry's budget bureau into the cabinet. In the latter half of 1958, the late Kawano Ichiro and others announced a concept of establishing a cabinet office and incorporating the budget bureau.

After that, concepts such as introducing a cabinet aide/cabinet participation system, or, at the time of the Miki cabinet, "giving the right to compile the budget to the minister's residence" have come and gone.

In this reorganization of the cabinet secretariat, the right to compile the budget was not given to the secretariat in one fell swoop. Nevertheless, the secretariat gained a direct hand in foreign policy and defense, will control information, and moved to divide the administration of the cabinet councilors' office which the Finance Ministry had controlled for generations.

Perhaps the Finance Ministry is not far off in warning that making the prime minister's residence into a White House "is an effort by the Nakasone-Gotoda line, old Ministry of Home Affairs faction to make the Finance Ministry relatively weak" (a vice-ministerial level Old Boy of the Ministry of Finance).

On 25 July, Prime Minister Nakasone practiced making his residence into a White House. Three days after the formation of the new cabinet, he called 11 bureaucrats individually to his residence, and indicated basic policy, decision methods, and goals concerning individual pending issues. He brought up separate matters, and gave a series of instructions, such as, "come up with a visible measure to resolve the economic friction with the United States before the U.S. mid-term election," "further reduce the high yen advantage on imported food items such as ingredients for soba, udon, and sushi," "bring the PTA in line with the times," "quickly realize the second stage of construction at Narita Airport," "work anew on the NLP issue on Miyake Island and on the issue of constructing U.S. military housing at Ikeko," and "formulate measures for our aging society."

Minister of Transportation Hashimoto and others came out gasping "I was canned up in the prime minister's office, and got squeezed."

Those close to the prime minister explain this unusual direct instruction from "President Nakasone" by saying, "his goal was to make a deal with the new cabinet members before they were brainwashed by office briefings. In any case, reform cannot be carried out unless the walls of bureaucracy are destroyed."

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## ECONOMIC

### FUTURE DIRECT U.S. INVESTMENT DISCUSSED

Tokyo KEIDANREN GEPPU in Japanese Sep 86 pp 2-25

[Roundtable discussion with Akio Morita, vice chairman of Keidanren, who is also chairman of Keidanren's International Industrial Cooperation Committee and chairman of the Sony Corporation; Hiroshi Kurosawa, leader of the A Group of Keidanren's U.S. Investment Mission, who is also vice chairman of the Industrial Bank of Japan; Mamoru Sakai, leader of the B Group of Keidanren's U.S. Investment Mission, who is also a director of the Japan Long-Term Credit Bank; Masayoshi Tozaki, leader of the C Group of Keidanren's U.S. Investment Mission, who is also the head of C. Itoh; Takushin Yamamoto, president of Fujitsu; and Masataku Okuma, Nissan Motors advisor]

[Excerpts] If Local Production Increases, the Strong Will Need To Consider Walking on Tiptoes

Yamamoto: There seems to be a certain type of reaction to Japan's overly visible presence. I feel that the U.S. side is suggesting that there are points we should take into consideration in the future. Expressions themselves, like "encourage" and "discourage," are too simple. The real situation is more complex. For example, even though we are welcome, if we attempt a bold step and go too far, we will face difficulties. Since people originally had the opposite way of thinking, at the same time I think we should engage in "compound eye" thinking.

In our case, we were welcomed by the local area, and I think that relations are good today, but if our production grows gradually in the future and our relative weight within the United States grows, we will gradually need to give consideration to the idea that "the strong should walk on tiptoes." Depending on the situation, I think we need to study joint ventures, that is, approach a U.S. partner. In fact, in the high-tech field, there is the phrase "computer nationalism" and the boasts of the people are strong. If we say, "What! You don't use a Japanese computer?" the Americans will remain silent. This is the same in Europe. Therefore, we decided to abandon producing large mainframes in the Fujitsu plant, and to organize Amdahl Corporation and joint ventures. NEC also recently decided to produce supercomputers in alliance with Honeywell, and I think that that sort of thinking may after all be necessary.

### Market Share First-ism Incites Friction

Yamamoto: The problems arising in the high-tech field now are in semiconductors. Mr Morita is providing much aid, but I think that is truly difficult. Only half of the problem lies in this area. Excessive capital investment and excessive competition based on that are not only causing destruction in the Japanese market but in the U.S. market as well. When we view the situation, I fear that we may be seeing the worst-case scenario now. At present our governments are showing wisdom and working toward an understanding, so I will refrain from making many comments, but I think that this sort of thing is deeply rooted in our social culture.

The trait of focusing on market share, expansion, and growth, rather than profits, will incite excessive competition any time. It is not that this does not exist in the United States or Europe, but it is a matter of degree. I think there is an extremely important point of trade friction in this. By all means, I would like to hear everyone's views on this afterwards, but I do think we must display wisdom by including everything from the problem of national characteristics with the tax system and other problems.

The basic causes of trade friction are two: friction that arises from excessive exports of goods, and friction that comes about because Japanese firms enter the market at a price at which local firms cannot compete. Looked at as a whole, the huge trade imbalance is a problem, and the complaint of individual firms is that they have not beaten Japan in competition up to now. Americans do not realize the kind of competition that goes on in Japan. The firms that have survived this set out for the United States and create the mood you mentioned a while ago. It is as if they are saying: "If he goes there, I will go there." As a result, the competition among domestic firms in Japan is brought over to the United States and a different kind of friction from that of today will arise, I fear. What does everyone think of this idea?

Okuma: As Mr Yamamoto just mentioned, this is the Japanese way of thinking about a product. Market share comes first, and profit is secondary. After all, as long as we build plants in the United States and Europe, and engage in work together with U.S. firms, this will not work well if both sides are not grounded in the same philosophy.

### Competition in "Software" Will Be Important in the Future

Okuma: In the case of automobile companies, I think that in the long term the issue is hardware, and in the functional sense, all the automobile companies in the world, whether slow or advanced, will all reach the same level. Therefore, I believe that the future international competitive power of the auto industry will inevitably require new technological development strength above the competition. I think that there will be a variety of these, such as new materials and electronics, and this new technology will have to be placed within an automobile and have a new function that a competitor's car does not. In short, we will live and die by technological supremacy.

One more thing, an automobile is considered to be a piece of fashion similar to a kimono. The owner is displaying his own being. Consequently, in addition to the superiority of the technology and the product, competition in "software" areas such as fashion may become important. Up to now, even though we have operated our plants at full capacity and taken a deficit with the long-term view in mind, the practice of selling our products at a cheap price to expand the market share at all costs cannot, in the end, continue forever. Consequently, I think we need to carry out a truly meaningful competition as I have just said.

With regard to entering the production market overseas, every company has made its decision with the foreknowledge that there will be a variety of problems such as the hollowing-out problem and a reduction of exports. Therefore, I believe that every company by all means needs to have the mental attitude that it is going to handle these problems by itself.

#### We Do Not Need To Bring Our Bloodstained Competition Overseas

Okuma: The thing we must avoid most is to conduct a bloodletting competition similar to what goes on in Japan in order to maintain operating capacity when the capacity utilization rate drops because of over-supply. It would be no mistake to frown on this.

Therefore, it is important to move wisely and seek sectors that should be specialized. This trend is emerging little by little. For example, the Big Three in the United States have been concentrating on large and medium-size cars and making big profits. Japan's automobile companies need to devise means to discover a new stratum of users by concentrating on small economy cars or by developing a novel car. In any case, I believe that we should, at all costs, avoid transporting to the United States our bloody battles that exemplify survival of the fittest.

Morita: Please excuse me for raising my company as an example, but Sony decided to enter the United States at the end of the 1960's, broke ground for its first plant site in 1970, and began production in 1971. We shifted to our idea that the source of supply should be where the market is located. However, recently, manufacturing in the United States has become a topic of discussion tied to trade friction and the strong yen. It would be good if we considered the problem from that aspect.

Tozaki: I think that I would like this issue to be considered truly and seriously from the viewpoint of an industry. For example, I believe that we must always keep the issue of local content in mind even if it does not appear on the surface or exist in law.

Judging this from the long term, Japan will undergo a hollowing out similar to the United States. That being the case, the competition among similar manufacturers will become more severe. We will probably need to seek an international code of ethics to combat this.

For example, let us take the case of the 256-kilobit RAM semiconductor. It fell dramatically in price from Y4,000 to about Y300. That is absurd, to put it mildly. I do not mean to criticize the manufacturers, but as in a Theodore White article which was published last year in THE NEW YORK TIMES MAGAZINE, the truth is that they have no choice but to become emotional over that.

Semiconductors: Where the Flaws of the Free Market Surface in Extreme Form

Yamamoto: Speaking from the standpoint of a manufacturer, the price of Y4,000 was really too high. The 256-kilobit RAM came into a seller's market because of a shortage, and the price was boosted upward. However, a price of Y300 yen is extreme. I do not think that all the semiconductor manufacturers are bad. After all, the price is determined by the market principle. There was no malfeasance on the part of the manufacturer. In this case, I think that the bad side of a free economy reached an extreme. Manufacturers provided a supply to where there was a demand, and pretty soon ended up with a supply surplus. As a result, the falling prices were part of the business cycle. I think that the present part of the curve we are on is on one end of the extreme. There is no truth to the accusation that the semiconductor manufacturers colluded to sell these cheaply. I believe that the price declined in line with the market principle.

Kurosawa: Where then did the paper come from on which was written the advice to "sell cheaper than U.S. products at whatever cost"?

Yamamoto: With regard to certain kinds of manufacturers, that is not just limited to the United States. That goes on constantly here in Japan. I believe that this can be viewed as part of Japan's corporate culture.

Tozaki: This is a question of international ethics.

Yamamoto: The fact that we all participate in Japan's corporate culture is not to be viewed with scorn. However, the "me-too business" in the United States is viewed with scorn. There is a great difference with Japan in that area. I think we need to give careful consideration one more time to the attitude of Japanese firms, which readily head toward excessive competition, when judging the issue of entering the international market.

Sakai: Of course, I think that in the process of entering the United States, the problem arises of Japanese corporations bringing to the local area their excessive domestic competition in its most naked form. As far as that is concerned, I am relieved that many of the Japanese firms which have entered the United States and whom I visited recently have blended extremely well into the local area. When I inquired about this with representatives of those firms, I was told that the idea of "corporate social responsibility" was somewhat different in the United States than in Japan. In other words, in the future the corporation will be sought to make a variety of contributions to the local area in ways other than business activities. There are a number of areas where the corporation is becoming an important participant, such as benefit work, the promotion of education, and the revival of the cities.

If we dismiss this role, we are apt to be criticized as economic animals even though the economic success of our enterprise is, of course, a prerequisite for any actions we might take.

Morita: The discussion has become one of corporate ethics rather than one of investment in the United States.

#### Size of Overseas Direct Investment by Use of a Level That Will Not Give Concern About Hollowing Out

Okuma: I know there is the problem of the hollowing out of our industries, but I think a bit differently on this. The other day I saw some data which stated that if one compared that percentage of sales from overseas production and sales from exports in the gross sales totals of several hundred U.S. multinationals with those of several dozen Japanese multinationals, you would find that 70 percent of sales of the U.S. firms were from items produced overseas and only 10 percent for Japan, whereas with regard to exports, the United States had a mere 10 percent, and Japan had 70 percent. Therefore, I think it is best to say that Japanese multinationals are export-oriented, whereas U.S. multinationals are international.

If we first consider the improvement of the present trade imbalance, I believe that our country should promote much more overseas investment, especially direct investment. I do not admire the view that direct investment overseas should be moderate because it will bring about a hollowing out of domestic industry, since that opinion only serves to dampen this trend.

Let us consider our automobile industry. This industry has an enormous number of employees and contributes greatly to employment. Moreover, the base of its related industries, such as the parts industry, is extremely wide. Were we to shift some production overseas, there would be a natural limit on how much we could do.

Moreover, there is the opinion that with the ratio of \$1 per ¥160, local-area production would be to the company's advantage. However, the production of automobiles, as you know, is extremely complex, and all sorts of factors are tied in. Therefore, we cannot simply shift to overseas production just because of a strong yen. There is the problem of quality, and there are other problems such as delivery and the productivity of the labor force. Production in the United States is not that simple.

If we look at the issue in that light, we are not yet at the stage where the government has to take some action with regard to the hollowing out problem. At the present time, entering overseas production is strictly to be carried out as a problem of our own company and on our own responsibility.

Morita: In an article that appeared in BUSINESS WEEK, the criticism was introduced that while it was good that Japanese firms were entering the United States, they would only be involved in screwdriver assembly-type operations.

Kurosawa: There is the statement that Japanese firms are "stealing work" from U.S. firms by linking up with their Japanese parts manufacturers, but I think that is a misunderstanding.

I am completely in favor of what Mr Okuma just said. If we take a look at the statistics for overseas production and domestic production with regard to the issue of hollowing out, we find that overseas production is 15 percent of the United States' total production, while it is 3 percent of Japan's. Japan's overseas production is still no subject for comparison. On the other hand, with regard to overseas investment, Japan is the number one overseas investor in the world, with \$10.2 billion invested the year before last (1984) and \$12.2 billion invested last year (1985). Of that amount, 33 percent, or \$2.8 billion, was invested in the United States in 1984, and 44 percent, or \$5.4 billion, was invested in 1985.

However, the reason that the percentage of investment in the United States is increasing is because of service industries, such as insurance, financial services, and real estate, and not much of that investment is in manufacturing. The percentage of investment in U.S. manufacturing was 35 percent in 1984, and a mere 22 percent in 1985. In short, 70-80 percent of investment in the United States is aimed at financial services, commerce, real estate, and insurance. It cannot be said that much is making its way into the actual establishment of factories. Looking at the total amount, we find that of \$25.2 billion invested, \$7.7 billion is going to manufacturing, or only 18 percent.

This figure of \$25.2 billion is still small when compared with other countries. It is just one-third of what Great Britain invested, and one-half of what the Netherlands invested. Consequently, although we must begin to pay close attention to overseas penetration, I do not believe that we have a risky situation that will bring about a hollowing out of our domestic industry.

#### Entering the United States As A Foothold to Becoming an International Firm

Kurosawa: One more thing. I asked several Japanese who were actually managing plants in the United States about the problem of how the Japanese could make a profit after showing up right after U.S. firms had decided they could not make any further profit and had shifted plants away from the United States. One answer I received to this was that it would be considered extremely embarrassing if, after all, they could not produce in the United States, and exports to the United States in such a situation became critical, if not impossible.

Moreover, it can be said that there is considerable merit to producing right in the immediate vicinity of the market while watching information and trends there.

Sakai: When all is said and done, the United States is an enormous ultra-modern market. If Japanese firms are to become international corporations in the truest sense, they by all means need to have a foothold in the United States. My feeling is that this is a natural trend.

In the financial world, as I am, one could not consider undertaking a full-fledged international operation for a minute without having a foothold in New York. The importance of the ultra-modern U.S. market is that it is extremely strong in marketing and high technology.

I recently saw from the sky the famous Research Triangle Park of North Carolina, and looking upon that breathtaking majestic high-tech base, I did not at all feel like making light of the United States in terms of hollowing out.

#### Tying Directly to the Market To Respond to Customer Needs

Morita: Mr Kurosawa has said this, but we began our production in the United States from the idea that we could produce goods that would match the needs of our customers by placing our production centers at places that connected them directly to the market. That is an important fact. Mr Yamamoto, isn't that increasingly true for the high-tech field?

Yamamoto: That is truly the way. Whether in computers or telecommunications, we in no way can create the market we desire with products designed in Japan. Rather, it would be best if we manufacture in, and export from, Japan items designed in the United States, but we cannot do that. Therefore, we have come to produce in the local area.

Moreover, we need to move production centers in the future to ease friction. Even if we sacrifice some profit, it is better that the trade barrier disappear and then we can enter the market. Therefore, we are not in a situation where we can neglect to encourage entry into the United States. And what is more, with the yen getting stronger, we have no choice but to be aware of the decrement of investment. There is always that risk.

Tozaki: You speak of a decrement.

Yamamoto: That is the decremented portion of the amount of investment when the yen appreciates.

Morita: That is a serious decrement.

Yamamoto: This is something that one must naturally watch out for.

#### Expansion of the Trade Imbalance Is Just the Flip-Side of the Japanese and U.S. Economies Becoming Closer

Okuma: The imbalance of trade between Japan and the United States has increased over the past 3-4 years, to be sure, but during this same period, joint ventures and cooperative relationships between Japanese and U.S. industries have become closer. A sense is emerging that the Japanese and U.S. economies are becoming unified. Even with regard to automobiles, U.S. manufacturers are steadily importing Japan's small cars and are selling them through their own distribution routes. Moreover, ties are drawing closer in the exchange of parts, joint development of manufactured items, and

development assistance and cooperation. About 30 percent of Japan's exports to the United States are said to be linked to U.S. business strategies.

Therefore, I have the feeling that the recent increase in trade imbalance may just be the flip-side phenomenon of the Japanese and U.S. economies becoming closer. If that is the case, we probably need to move that forward steadily. If the Japanese and U.S. economies and industries cannot do without one another, then a considerably different perspective is emerging with regard to the trade friction problem.

However, the current problem, as we all know, is that Japan has become the parts supply base for the United States. U.S. automobile and electronics manufacturers are steadily buying from Japan because the quality is superior. This has occurred because of the hollowing out of manufacturing industries in the United States. If this does not improve for the United States, the situation will be bad, I believe, no matter how hard Japan tries.

#### Stability of Exchange Rates Is the Prerequisite for Devising Management Strategies

Morita: Because the dollar had been strong for a considerably long time, U.S. managers shifted their supply bases overseas, where goods could be produced cheaply. Now it is not so simple to say that because the dollar is weak, the supply bases can revert to the United States. However, I do think that should this situation of a weak dollar and strong yen continue for a considerable period of time, the United States will increase its investment in domestic production facilities.

However, I recently talked with a certain U.S. banker, who let loose with the reckless remark that "It is OK for the United States to buy manufactured goods from foreign countries even if it does not produce any." If that is to be the case, the United States will soon no longer be an industrial country.

However, prior to such an argument, I believe that stabilizing the exchange rates is vital above all else. Some Japanese managers are transferring production sites to the NIC's [newly industrialized countries] where manufacturing costs are cheap, since they cannot figure out the future course of exchange rates. What do you think of this problem?

Tozaki: What must be clearly recognized is that international borders are crumbling when it comes to trade. Moreover, this trend is likely to continue, for better or worse. Corporate leaders have no choice but to deal with that fact as a prerequisite in their decisionmaking. If that is the case, I am afraid that in the final analysis Japan will undergo a hollowing out. The trading companies understand this the best. They have no sense of international borders. At the present time, their headquarters happen to be in Japan, but if the truth be told, they do not need to have them in such a place where taxes are high.

Even in the United States, corporate taxes are just 33 percent. Moreover, there are places in the world where the corporate taxes are close to zero.



This is the same with personal income taxes. When we consider that, what sort of need is there to stick to international borders?

U.S. companies are currently heading in that direction. Pardon me for mentioning names, but the first thing David Roderick did upon assuming the chairmanship of U.S. Steel was to transform U.S. Steel from a steel company into a chemical company. He shifted it to the downstream chemical product and plastic areas. I was stunned at the time. This was U.S. Steel, after all, which had dominated the world for such a long time. Subsequently, U.S. Steel purchased an oil company and now has changed its name to USX Corporation.

Recently I met Roderick and told him: "At first, I had my doubts about your management policies, but I have come to share your feelings about the company." He was extremely pleased upon hearing this. I thought it was truly splendid for a steel company fighting for the number one or number two spot in the world to go as far as it had.

Morita: Mr Kurosawa, how does that kind of phenomenon appear to you as a banker?

#### Stabilization of Exchange Rates by Macroeconomic Policy Coordination Rather Than by Reform of the System

Kurosawa: A short while ago Mr Morita made the statement that "we will have extreme difficulty either exporting or investing if exchange rates are not stabilized." How well I understand what you said! However, opinion is unanimous among monetary authorities that while the current floating-rate system is not the best, it has fewer flaws than the other systems. Returning to the gold standard would be extremely difficult.

Because intervention worked well for a short time after the G5 agreement last September [1985], some persons spoke out about the negative target zone concept and other ideas, but the situation soon worsened. I think that artificially suppressing natural fluctuations of currency value is senseless, no matter what system is adopted. Of course, the most troublesome item for an overseas investment is the decrement of the investment. Were we to convert investments made when the dollar was worth Y360 to their current value, it would be less than half the value of that time. Regrettably, no good plan exists at this time to resolve this dilemma.

Sakai: As you have said, exchange rates under the floating-rate system, as far as one can tell up to now, have repeatedly risen and fallen chaotically, and by no means can be considered stable. For exchange rate stability, after all, the economic management of both Japan and the United States needs to be conducted more smoothly. In the United States, something must be done about the fiscal deficit. This, regrettably, will take time. Corporations need to wait a while longer for the exchange rate to calm down and then for the economic environment to stabilize.

Yamamoto: If I may speak from the viewpoint of an industrialist, our feeling is that the rate of the yen's rise is too sharp. If there is no good means

of handling this other than the floating-rate system, we can only carry on by means of economic principles.

I think that the honest solution is not for the United States and others to produce factories but for the NIC's to do so. I think it will be quite natural for some sort of boomerang effect to occur, or, in any case, for the NIC's to become sites for new plants, and as a result, for the NIC's to develop and for world trade to expand.

However, according to Kunio Kanamori of the Japan Economic Research Center, when \$1 equals Y157, the per-capita GNP of Japan will be close to that of the United States, and the possibility will emerge that building factories in the United States will be cheaper than building them in Japan from that point on. This is because land, housing and energy will all be cheap.

From now on, when it comes to the problem of decrement of investment, along with reading the trends of exchange rates, one must be resolved to invest with that much risk.

Tozaki: I think that if the market share for manufactured goods in the United States were guaranteed to a certain extent, excessive competition among companies in the same industry will disappear and orderly sales can take place, because it is so large a market. If that is the case, I think that while there may be some decrement of investment as a result of entering the U.S. market, we need not be disconcerted.

Morita: We should greatly encourage investment in the United States, but, on the other hand, the behavior of Japanese firms that have invested is becoming a problem.

Tozaki: It is just as you say. I think that competition among firms in the same industry will be a particular problem. If U.S. firms as well as Japanese firms decide to act in harmony, then I think that investing in the United States is a good idea.

Toward an Era of Detailed Concerns Over Institutional Factors Like the Tax System

Morita: Returning to the issue of corporate ethics, if that is the case, then when will the behavior be good? As long as investments in the United States increase in the future, the conduct of Japanese firms will receive attention. What was written in that article in BUSINESS WEEK may be considered, I feel, testimony to the fact that some alarm is appearing over the inroads made by Japanese firms.

Tozaki: The EC is even more severe. Let me raise the VTR issue. The people over there became possessed with the idea that every item brought over from Japan was being dumped. It was that great of a problem. Consequently, we have many joint ventures with the EC. We had no other choice but to do that.

Morita: As President Yamamoto said a while ago, tie-ups with local firms are a means of avoiding antagonism and useless friction.

Yamamoto: However, when we speak of our manufactured products, we do not mean that the Japanese stand in the front line of sales. We are seeking the forbearance of all the people of the local area. Consequently, I think that a certain amount of orderliness is expected to be maintained.

The problem is the export price from Japan. Of course, there is the problem of partners, but the real problem is the export price from Japan.

This has been pointed out by Sofia University Professor (Abblegen), but in Japan, even though no tax is levied on capital gains, shareholders and managers work hard to maintain the price of a stock because dividends need to be kept up regularly. As a result, market share expansion, which has a great impact on the share price, has become an objective. Following this, there is the sense that the era has arrived when we must also give detailed consideration to institutional factors.

Tozaki (with a smile): At the same time, we can say that major shareholders like financial institutions treat management in a generous manner. More accurately, they treat firms as long-term prospects.

Yamamoto: This accounting period we suffered a considerable reduction in earnings, and the shareholders pressed us with questions. However, we naturally expected to receive this. If this were the United States, I think we would have been castigated more severely. Japan is a comparatively tolerant country over this.

#### Fostering Local Parts Companies Becomes Important

Morita: We have discussed automobiles, but we have many cooperative companies. Once a major company goes overseas, all its cooperative companies follow in its footsteps. That being the case, the Americans dislike it intensely, but when they argue that it would be best if just the parent company come and use locally manufactured parts, we have in many cases suffered from quality and other problems. When that happens, they angrily cry that "Japanese firms will only buy from their affiliates." I think that this sort of problem is a latent one that must be resolved in the future.

Okuma: We need to be fully aware of this problem over there. We cannot reasonably expect to have in the United States the parts supply system that we have in Japan. If we speak of automobiles, because the automobile manufacturers and the parts manufacturers have an extremely close cooperative relationship, whether capital is being invested or persons are sent overseas on technical guidance, they maintain an extremely strong and close-knit relationship. The U.S. side has a problem with that, and makes the criticism that "Japanese firms will only buy parts from keiretsu companies." If that type of system is carried over to the United States, it will inevitably be knocked down. We need to construct a system for purchasing parts from U.S. companies.

However, that is something of a problem. The portion manufactured by the automakers themselves in the United States is a markedly higher percentage than that of Japan. The percentage produced by Japanese manufacturers is low because of historical circumstances, and consequently, the percentage purchased from outside suppliers is high. Therefore, even if we go to the United States and attempt to buy parts, they are not available. That being the case, Japanese automakers and parts manufacturers have no choice but to go together to the United States.

Nonetheless, if we want to enjoy the merits of the strong yen, it will have no effect unless we purchase locally-produced parts. If we proceed to make many purchases of local parts, I think we will naturally resolve the local-content issue.

Yet the problem, as you have just said, is that their prices and parts do not meet our conditions and various kinds of parts are largely unavailable. Therefore, it is important that we skillfully rear these parts companies.

Yamamoto: In a sense, this is probably a form of cultural friction. The relatively low percentage of domestic manufacturers is also true for the electronics industry. This is not just the case with automobiles but across the board. As Mr Okuma has pointed out, we must pay great attention to this.

Morita: If I may raise an example of my own. We have fostered small local firms as cooperative companies. However, when large firms attempt to venture out from this, they cannot say to the cooperative companies that "it would be difficult for us to have you enter the market." Since these are cooperative companies, I think it would probably be best to say: "We also want to enter the market."

Kurosawa: This is because if there is no parent firm, there will be no work.

Morita: One investment in the United States brings on a variety of problems.

#### Maekawa Report and Overseas Direct Investment

Yamamoto: Growth industries are placing new factories overseas and not just in the United States. However, mature industries cannot move overseas without causing a decline in the capacity utilization rate of their domestic plants. The reality is not so pleasant when they largely promote overseas investment and a domestic hollowing out becomes inevitable. This is because they cannot move overseas unless they close domestic factories. We may be entering an era, in the case of mature industries, where that should be considered.

Tozaki: The problem is that this is not in line with the Maekawa Report. The Maekawa Report declares that we should adjust our economic structure over a 5-7 year period and shift away from an external demand-driven economy to an internal demand-driven economy. The export dependency of our country's firms is over 30 percent. For some of them it is 50-60 percent. We may have no alternative to a hollowing out as we attempt to be an internal demand-driven economy. This is because exports will gradually disappear.

Okuma: There is the hand of multilateralism in this.

Kurosawa: I think the Maekawa Report has some problems.

Tozaki: However, the United States is highly pleased with the Maekawa Report.

Kurosawa: The emphasis of the Maekawa Report is to aim at Japan's being both an export superpower and an import superpower. Now, when it comes to Japan being an export superpower, exports only hold a percentage of just over 10 percent of the GNP. That is not so great. South Korea's is 49 percent. Taiwan's is 50 percent. Even some European countries are around 30-40 percent. Therefore, I do not think that Japan can be called, by any means, an export superpower. Yet, if we take up individual industries, such as electronics and automobiles, exports occupy 50-60 percent of the total and give the impression that our exports are high. The Maekawa Report inadequately covers this. In the first place, there is a misunderstanding in the United States about our economy. I think some problems arise when they get a free ride without having that impression corrected.

I think I would like to have a U.S. version of the Maekawa Report written in the United States. For example, the U.S. trade deficit with Japan was about \$20 billion in 1979-1980, but I would like to know why that exploded to \$50-60 billion during these past several years. Since our trade barriers did not increase at all during that time, I have determined that the cause is over there.

Tozaki: There is the Young Report in the United States.

Kurosawa (laughing): I would like to hear an explanation from the other side.

Tozaki: The United States had to switch its line from that of Treasury Secretary Regan and Under Secretary Sprinkel, which it had followed for 5 years, to that of Baker and Darman. The people over there are saying: "We have been patient for 5 years now."

Kurosawa: Even though they claim to have been patient, that is because they were pleased. They did as they liked, saying: "Strong dollar, strong America."

Tozaki: Say what you want, Regan did not change his policy.

Kurosawa (laughing): That it did not change was the mistake of the other side. I would like to give him a word of thanks.

Sakai: Isn't this because American politicians always base their views on extremely simple and clear-cut theories and try to draw the majority of the people to their side? I feel that the concept of such a style being a form of political leadership is extremely strong. As a consequence, when the details of the policy are inadequate and the failures pile up and the policy soon seems bad, the policy wavers. This is far more the case in the United States

than in Japan. For example, I feel that supply-side economics reached center stage but now is no longer seriously discussed.

Yamamoto: When the dollar became cheaper after 22 September 1985, U.S. exports did not surge. I think that is the problem.

Kurosawa: U.S. exports have not increased at all. The trade deficit has never declined. The decline of exports from Japan is not tied at all to an improvement in the balance of trade because exports from South Korea and Taiwan increased.

Tozaki: However, the United States worked hard to pass Gramm-Rudman, even though it violated the Constitution. At the same time, Federal Reserve Bank Chairman Volcker has repeatedly stressed that maintaining the value of the dollar is essential. In that sense, I think that the United States is aware of the importance of the situation.

Kurosawa: Knowledgeable people understand the situation.

Tozaki: That being the base, I think that both deficits, especially the balance of trade deficit, will gradually decline.

Kurosawa: If that is so, wouldn't it be good if we waited awhile until the deficit dropped?

Tozaki: There is the view that Japan and the United States should consult on the exchange rate issue, but nothing can be done if this is not studied together with the problem of the exchange rates of the countries of Southeast Asia. This is because although trade between Japan and the United States has steadied, the United States is developing a deficit of over \$20 billion with the Southeast Asian nations.

#### Direct Investment in the NIC's Becomes Important

Kurosawa: President Yamamoto just said it, but I too believe that investment in the NIC's will become extremely important. At present, 37 percent of our exports go to the United States. If we wanted them [U.S. customers] to buy 40 percent, we would have to listen to them say, "Good, we understand," even if the logic used to persuade the customer was crazy. Moreover, 80 percent of our surplus comes from the United States. Even when they complain absurdly about this, we cannot rebut them. That is somewhat extraordinary.

On top of that, when the dollar becomes worth Y160, we will shift our product lines to South Korea and Taiwan. Because South Korea and Taiwan cannot export without receiving parts from Japan, this will be convenient for them. If exports from South Korea to the United States increase and the percentage of exports from Japan decreases, the situation may improve little by little as the United States will have nothing to say as it does now and we will have to go along with that.

Yamamoto: If the dependency of our nation's industries on the United States improves, then the scale of the world's economy will expand.

Kurosawa: This will be because of Asia, not only Japan.

Yamamoto: In the case of South Korea, although imports from Japan may increase, exports will increase beyond that.

Morita: Investment in the United States must be encouraged, of course, but we need to consider indirect investment in the United States through the industrializing nations.

Yamamoto: I feel this is as important, if not more important, than investment in the United States. Rather, from the standpoint of tariffs, the NIC's may be more important.

Oluma: We may be gradually heading in that direction.

Yamamoto: This type of phenomenon is appearing here and there in the form of putting up factories in Taiwan and South Korea.

Tozaki: However, some countries among the industrializing countries are receiving heaps of international criticism for just receiving the benefits of trade without fulfilling their obligations.

Yamamoto: I think like Mr Tozaki. For example, even if we transfer technology to certain countries, we are restricted by such problems as royalties. It is necessary, even if it comes about slowly, that Japan not just negotiate with the United States but talk with the NIC's as well. Both the government and Keidanren must strengthen their awareness of the NIC's. After all, I think we should have a discussion as follows: "We will give you technology. We would like to know what you will provide in return."

Tozaki: In the present situation, just because we move into NIC markets does not mean we can solve the problems. This is because they attach all sorts of conditions. After taking that into full consideration, I think we should decide to invest in the NIC's.

Sakai: I think it is just as you say. Around this year, a type of three-sided relationship--not just the Japan-U.S. relationship--of Japan and the United States, Japan and the NIC's, and the United States and the NIC's may have come into the spotlight. Because virtually all of the NIC's of Latin America and Asia are dollar-linked countries, they have been anticipating increased exports to the United States after the rise of the yen. However, there is also the view that the United States was annoyed when imports from the NIC's increased excessively and its own trade deficit did not decline, so it will apply some sort of pressure on the NIC's. We may be entering an era in which Japan's overseas investments must be considered within such a complex process of alliances.

Morita: The problem of overseas investments needs to be considered not just from the standpoint of investments in the United States, but from the overall picture. Therefore, from a global perspective, we probably need to reexamine our approach toward industrial structure and to improve the means applied up to now.

Tozaki: In short, at present when international boundaries are vanishing, the feeling is spreading among managers that they are running multilateral firms. Moreover, in each sector, the need for detailed study is becoming greater.

Kurosawa: A while ago, Chairman Tozaki referred to the behavior of financial institutions. I think that we must take this to heart. Recently, in New York, I heard it said that a U.S. investment bank suffered a heavy loss because of a Japanese firm.

Tozaki: A similar incident is said to have occurred in London.

Morita: We need to have an ethical viewpoint that can be applied worldwide.

#### Entering a Market in a Way That Will Improve the Local Quality of Life

Okuma: The problem of ethics arises when the behavior of the firm entering the market becomes a problem, and other than that, personal behavior is the problem. Which one it is is important. Even though firms enter markets, it is men who actually perform the work.

The expression "quality of life" does not have an accurate translation in Japanese. That is to say, the quality of life concept is not a traditional one for the Japanese. However, after going to the United States and working there, I can clearly understand what quality of life means. We need to respect that and contribute to the society of the local area.

Kurosawa: That is so. Because a Japanese firm has entered a local market, it needs to improve the quality of life of that area.

This is a joke, but there are three points when it comes to deciding where to locate a factory. First, are there Japanese restaurants? Second, is there a Japanese school? Finally, is there a golf course? Because VIP's from headquarters come occasionally, it would be difficult if there were no golf course. (laughing) There is a considerable gap between the quality of life of Americans and the feelings of the Japanese.

Okuma: Even the idea of market share first is probably an idea that every Japanese has come to accept from the past. As a result, I think this has a relationship with education. Consequently, we are educating people who can think more internationally. If we can alter our education in that direction, I think we will achieve a basic resolution of such a problem.

Kurosawa: It is bad just to educate the men who are going overseas. After all, there is a need to accept as many foreigners as possible in Japanese



society. Even on the issue of school teachers, we say in the end, after all the hullabaloo, that "we do not care if it is just a language teacher." Rather, with regard to foreign teachers of foreign languages, we had a more substantial number before the war. Therefore, this is a harsh statement in this regard.

Tozaki: It is a difficult problem.

Kurosawa (laughing): It is groundless to assume that, in the country of Japan where the only people who eat Japanese food, play golf, and play mah jong are Japanese, these same people will suddenly go to Oregon and become international.

Yamamoto: Everyone suffers in the factory contingent.

Tozaki: I think it would be considerably different if the managers of the Japanese firms entering the local market met on occasion and just exchanged information.

I know we talked about Oregon, but Japan has traditional ties there. Grain has been bought from Oregon for a long time. Our company established its first two branches in the United States in New York and Portland, Oregon.

Yamamoto: Lumber is there as well.

Tozaki: Yes, Oregon is extremely close to Japan. When the unitary tax was abolished and firms, beginning with Fujitsu, moved in there, that was a really good thing. If I may speak for myself, I lived together with my family for almost 2 years in Portland.

Morita: The unitary tax problem must be resolved by all means, and we cannot go on thinking that the problem is California alone.

Tozaki: It is troublesome.

Morita: I think it is strange that a state has the authority to cross international borders and levy a tax. This is a violation of sovereignty. I think it may be good to have the government take up and negotiate this problem.

Tozaki: The same thing can be said with regard to accountants and lawyers. Regulations differ between the states and the federal government. The authority of the states is strong in the United States, and the rules differ according to the state. That is a weakness.

Morita: I would like to have the Japanese government treat this problem a bit more seriously.

Tozaki: Instead, Great Britain is doing all it can to deal with it.

Yamamoto: I would like to have the Japanese government itself be more internationalized. It always negotiates defensively with its hand tied behind its back. I would like it to negotiate on a more even basis in the future. Consequently, we need first to start from a consciousness-raising revolution.

Morita: Because firms have internationalized this far, the government had not considered going that far.

Yamamoto (laughing): Therefore, the internationalization of politicians is necessary.

Morita: This is because the companies have moved ahead without waiting.

Tozaki: The criticism that "Japan is violating the GATT" and "is violating international treaties" is most disturbing. The government is involved in many cases of this, and both the government and all the ministries and agencies should take care that this sort of thing is not said.

Morita: Is there anything else that can be done?

Sakai: During a recent trip to the United States, officers of a Japanese firm there said they wanted to convey something to the government of Japan by any means possible. This was the issue of overseas education of children. For example, this includes the expansion of supplemental Japanese-language schools, the dispatching of outstanding teachers, the drafting of excellent educational materials, and improvement of the atmosphere for accepting the children when they return home. It is readily apparent that Japanese firms will internationalize from now on, and while this may be a minor thing, it is important. I would like the government to tackle this question seriously.

Morita: That is so. Mr Yamamoto, what do you think?

"Excessively Deregulated" United States Vis-a-vis "Excessively Regulated by Jurisdictional Disputes" Japan

Yamamoto: The United States is moving ahead with deregulation, and it predominates as the investment environment, but if I can speak from the standpoint of a telecommunications equipment manufacturer, I am certain that as a result of all sorts of regulations being eased or abolished, participation in the market will become easier, and an invigorated business atmosphere will emerge.

Okuma: With regard to deregulation, the United States is revising the laws related to ocean shipping 2 to 3 years ahead of time. Since I manage an ocean shipping company, I largely introduced the principle of free trade that we have not needed up to now because of regulations in the form of the shipping conferences that exists today. However, containers on the Pacific lanes subsequently went through a lot of trouble. They all rushed to compete by lowering the shipping costs, and everyone suffered a deficit.

Although it is fine that deregulation advances, what, in short, is it aimed at? I think that the result of the easing of regulations will probably be a world of survival of the fittest. U.S. shipping companies, as a result of the survival of the fittest, may be scheming to be able to ensure a considerable share.

Morita: The deregulation of the United States is thorough. If I may talk from my experience as an official of Pan Am, the airline companies are being ruined one after another. If we carry out deregulation to that extent, will it, after all, be for the good of the general public? Areas of doubt are emerging.

Compared to that, Japan is over-regulated. Even with regard to banks, Japan has the idea that they must not fall apart, but the United States clearly discerns that it is bad to make deposits in a bank that will fail.

Tozaki: This is troublesome in the case of Japan because it is strictly an attempt to let vested interests persist.

Morita: The thinking in vogue in the United States is to challenge a variety of things at one's own risk. Japan is different. Were some sort of emergency to occur, responsibility toward the nation would immediately be carried out. If that is the case, the process of deregulation is different in virtually every area.

Okuma: There are a variety of regulations even in the fields of biotechnology and life sciences, and these are reported to be a hindrance to research activities. Since these are extremely desirable fields in terms of the 21st century, we would like the regulations to be eased and the research results to be appreciated.

One more problem is that jurisdictional disputes between ministries and agencies occur because of the various governmental relationships. We are in a dilemma. I entirely believe that we must improve such a thing.

Morita: Jurisdictional disputes among government agencies also exists in the United States.

Okuma: We may be arriving at a good era from the standpoint of creating an organization to adjust the interests of the various government offices.

Morita: If there becomes a problem with regulations, the inadequacies of Japan meet the eye right away.

Okuma: Joint research among industries, the government, and the universities does not progress because it is tied to regulations and the violent jurisdictional disputes among government agencies.

Morita: The industry, government, and university joint-research system is clearly moving ahead in the United States. However, in the case of the United States, exchanges of personnel among industries, the government, and the

universities are going on daily, and the boundaries among industries, the government, and the universities are not too clear. Because these boundaries are cut more clearly in the case of Japan, not much joint research is moving forward.

Today, we have spoken for a long time, and I would like to thank you all for being here.

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## ECONOMIC

### JAPAN-PRC TRADE EXPANSION COUNCIL OFFICIALLY INAUGURATED

Tokyo NITCHU KEIZAI KYOKAI KAIHO in Japanese Sep 86 pp 4-6

[Excerpts] The general conference for the establishment of the Japan-China Trade Expansion Council was held in the Hotel New Otani in Tokyo on 9 September, with approximately 150 representatives of economic bodies and enterprises supporting the establishment of the said council in attendance.

#### Sino-Japan Trade Alone Drops

As is generally known, Sino-Japan trade last year showed a deficit of approximately 6 billion dollars on the Chinese side, and this year not only did this steady deficit trend on China's part not change, exports and imports alike manifested a stagnating trend. Japanese exports to China during the first half of 1986 came to 4.588 billion dollars, a 23 percent reduction from the same period last year, while imports from China came to 2.878 billion dollars, a drop of 9 percent. Thus the export-import total came to 7.466 billion dollars, a drop of 18.5 percent over the same period last year.

On the other hand, China's world trade figures showed growth in both exports and imports during the first half of 1986. According to Chinese customs statistics, exports during the first half of 1986 came to 13.53 billion dollars, an increase of 14.4 percent, while imports totalled 19.9 billion dollars (an increase of 8.6 percent), and the import-export total came to 33.43 billion dollars (an increase of 10.9 percent). Looking at this by region/country, import-export totals between the European Community (EC) and China came to 5.271 billion dollars, an increase of 53.7 percent; import-export totals with the U.S. came to 3.631 billion dollars, an 11.5 percent increase; and import-export totals with the Soviet Union came to 1.008 billion dollars, a 58.3 percent increase. Thus we see an across-the-board increase with all these areas. Judging just from statistics, the amount of the drop in Sino-Japanese trade is more than the increase in trade with Europe and America, particularly EC countries and the USSR/Eastern Europe. With the continuing strong yen/cheap dollar situation, the amount of trade between China and Europe and the U.S. is growing, while for the time being in trade with the USSR and Eastern Europe open account transactions--which do not require foreign exchange--are increasing. During this period, only Sino-Japanese trade dropped, and this is a fact that bears watching.

In that sense as well, the establishment of the Japan-China Trade Expansion Council is significant, as the aim of this council is to develop economic relations between China and Japan, based on the expansion of imports from China.

#### Present Operational Plan

The basic policies of the council as agreed upon with the Chinese side are as follows:

1. For China to continue to develop export products in the future, certain manufactured items which can serve as models in this area will be designated, with comprehensive model enterprises promoted whose goal will be the systematic development of such products through various stages, including product planning, market surveys, introduction of technicians, improvement of plants, and hosting of trade fairs and export conferences.
2. Promote the spread of fundamental know-how indispensable to the smooth development of trade/industry, such as trade and financial practices.
3. Provide all possible cooperation in the establishment of export commodity production bases and export-oriented factories, which the Chinese have cited as goals of the seventy 5-year plan.
4. In addition, carry out personnel exchanges and technological transfers related to the development of new products, the improvement of commodity delivery, and the upgrading of processing technology, design and quality control to be carried out by the Chinese by various commodity sectors.
5. Regular exchanges for the exchange of information and opinions.

In addition, the present operational plan is as follows:

1. Issue invitations to policy makers. Invite to Japan those individuals from China's Ministry of Foreign Trade and other governmental agencies and trade companies, etc., who are responsible for policies on trade with Japan, so that they may have wide-ranging exchanges of opinions with their Japanese counterparts concerning follow-up operations to the establishment of the trade expansion council, as well as concerning the Sino-Japan cooperation system.
2. Send specialists in trade and finance practices. Send missions made up of trade and finance specialists to promote China's modernization through the construction and improvement of export bases and export factories, providing wide-ranging cooperation in such areas as know-how regarding expanding exports, technological guidance, quality control, infrastructure improvements and financial cooperation.
3. Send survey teams to China to check on local conditions. a. In keeping with the establishment of the trade expansion council, send survey teams to China centered around the Planning Subcommittee to carry out exchanges of opinions with the Chinese Ministry of Foreign Economic Relations and trade and other concerned agencies concerning the implementation of various operations

related to the expansion of trade. At the same time, carry out surveys of China's export base and export factory construction, and other such export promotion policies, ascertaining local needs and collecting information for the formulation of comprehensive plans as follow-up measures for the future.

b. Formulation of plans, Convene ad-hoc study groups to implement effective trade expansion follow-up operations (including 102 items proposed by the Chinese), and formulate comprehensive plans or planning by commodity subcommittees.

4. Sending missions by industrial classification. a. Formulate individual plans in commodity subcommittees in keeping with the situation by commodity or by industry. b. Formulate cooperative project plans.

5. Model operations. Carry out liaison/coordination related to the trial purchase survey(s) to be carried out by the Japan External Trade Organization (JETRO).

6. Other. a. By sending consultants to China and holding export promotion seminars, lectures, etc., in China, explain the situation in the Japanese market and strive to promote exports to Japan. b. Inviting production managers to Japan. In order to improve the quality of Chinese manufactured items, invite specialists from China's export businesses and export-related companies to see related agencies in Japan, carry out technical exchanges and, in addition, carry out surveys of the actual situation as concerns the expansion of exports to Japan from a technological standpoint.

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## ECONOMIC

JAPIA CHAIRMAN ON DIRECT OVERSEAS INVESTMENT, MOSS

Tokyo KEIDANREN-GEPPU in Japanese Oct 86 pp 35-40

[Yasusada Nobumoto, Chairman of the Japan Auto Parts Industries Association and President of Akebono Brake Industry, is interviewed by Katsura Kuno, head of Keidanren's public affairs department]

[Excerpts] Parts Manufacturers Help Make Excellent Cars

[Question] To begin, would you please give a general overview of the auto parts industry.

[Answer] The characteristic feature of the auto parts industry, to sum it up in a single phrase, is its diversity and breadth. The 387 member companies of the Japan Auto Parts Industries Association make a truly diverse variety of parts, from engine and brake parts, to seats, measuring instruments, windshield wipers, horns, electrical system components, and car air conditioners. And the size of our member companies ranges from giant corporations to medium and smaller businesses.

Total parts production has risen steadily from 5.965 trillion yen in 1980 to 7.221 trillion yen in 1984, and in the last two or three years it has been growing at over 10 percent a year. By categories, body parts account for 27.2 percent of the total value of parts produced (1984 figures), followed by electrical system components (20.7 percent), drive train, transmission, and steering mechanism parts (15.8 percent), and engine parts (14.6 percent).

In terms of jobs, the auto parts industry as of 1985 employs about 480,000 people.

[Question] I understand that about 60 percent of the parts used by Japanese automobile manufacturers are supplied by manufacturers which specialize in parts.

[Answer] It varies with the auto company, but in general 60-70 percent of the parts are supplied by parts manufacturers. One may well say this is a feature of the auto and auto parts industries in Japan; in America auto parts are made to a great extent by the automakers themselves. In other words, the rate of self-production in the auto industry is much lower in Japan than in America.



This is one reason why our auto industry is so competitive internationally: because the parts makers all strive to hone their technology, keep costs down, and stay ahead of their competitors.

#### Politics Comes First in U.S.-Japan Relations

[Question] What about the trends in auto parts exports?

[Answer] Exports doubled from 883.2 billion yen in fiscal 1980 to 1.9857 trillion yen in fiscal 1985--that's about 30 percent of sales. Regionally, exports to North America, which until 1982 were about one-fourth of the total amount, have risen rapidly to 40 percent in 1985.

There are two reasons for this increase. One is the fact that Japanese parts manufacturers are the major source of parts for small cars, and the demand for small, fuel-efficient cars has grown worldwide following the oil crisis. The other reason, of course, is that Japanese parts are very well-made and reliable.

[Question] But aren't foreign-made parts being used more and more?

[Answer] I think politics has something to do with that. Auto parts are one of the items on the agenda of the MOSS conference between Japan and the United States, and they're having to buy foreign-made parts because of political pressure.

[Question] But the quality of auto parts affects safety. Is it proper that automobile manufacturers should buy such parts merely for political reasons?

[Answer] Your point is well taken. But in U.S.-Japanese relations the fact is that politics comes first, and economic principles are not followed very much.

#### Joint Ventures to Avoid Investment Friction

[Question] Will parts manufacturers set up operations overseas as automakers shift their production facilities to overseas?

[Answer] That's a difficult problem, and in general we can't say. As you might think, the most important thing is that automobiles made by Japanese manufacturers in foreign countries must have the same quality as their vehicles made in Japan. Sales of U.S.-made Volkswagens once suffered because the ones made in America were of much poorer quality than those made in Germany. The technology of Japanese auto parts manufacturers is needed to ensure that that doesn't happen with Japanese cars. So even before the yen started to rise in value we were setting up operations overseas.

In doing so, I think it's desirable for the companies setting up foreign operations not just to create employment but also to cooperate with existing local companies in technology and capital. The latest issue of Business Week uses the phrase "investment friction," and there are those who say that Japanese companies setting up operations in other countries do not create jobs

but are stealing jobs. By "stealing jobs" they mean that every time a Japanese company builds a factory in a foreign country, the survival of an existing company is put at risk.

[Question] Generally, we often see an attitude of welcoming with open arms investment from Japan, but that seems not always to be the case any more.

[Answer] Akebono Brake is building a factory in Kentucky in a tie-up with GM. I took the decision to do this as a joint venture, even though it would have been less troublesome if we had done it on our own, since we would have avoided the old, traditional style of labor-management relations.

[Question] Do you think it's better to make use of the personnel and sales force of an experienced partner company, rather than starting from scratch?

[Answer] Certainly that's a consideration.

#### The Domestic Auto Market Is Still Growing

[Question] As automakers advance overseas, what will parts makers have to do to cope with such developments?

[Answer] Not everybody can set up operations overseas, because doing so involves all kinds of capital, personnel, and other problems. As local production of cars overseas is increased, domestic production might go down, and a shrinking domestic market would present the parts industry with new problems to deal with. We must rather think of expanding the market. This is a problem not just of automobiles; it involves the great problem of how to convert the entire economy of Japan from one which depends on exports to one which is led by domestic demand.

But the domestic auto market still has room for expansion. There is a growing number of people who say, "Well, we might not be able to afford a home of our own, but at least we want a car," so we can expect further demand. I am not pessimistic about the future of the automobile industry.

[Question] So you foresee a large market even just within Japan.

[Answer] Yes. There may be no growth quantitatively, but we can expect qualitative changes. For instance, we'll see easier-to-drive or more stylish cars embodying electronics or other new technology. Or we might see different kinds of cars made for different age groups. There are still plenty of possibilities.

#### The Government Underestimates the High-Yen Problem

[Question] What do you think of the current situation with the high value of the yen?

[Answer] When I watched an interview program on television recently, there was Prime Minister Nakasone saying proudly, "strong yen, strong Japan." He was

saying that with the country's currency strong, at 150 yen per dollar, the whole Japanese economy is that much stronger. It's no joke. With the deflation caused by the strong yen, we see before us domestic consumption falling and GNP stagnating. I think it's a big mistake to consider it a success to have brought about a stronger yen. We must, through Keidanren, stress this point to the government and get them to change their perceptions.

The government has been very slow to react and in many cases has made the situation worse. The situation we have today is in part due to the government's inaction despite the signs of an intensification of friction that have been apparent for some time. Because of that, the G5 [group of five] agreement was reached in September of last year to make adjustments for the strong dollar, and since then the strength of the yen has escalated. The government seems to have thought that the strong yen would last only until the Tokyo summit in May, but once that summit started, none of the participating countries recognized the necessity for doing something about the strong yen. The government never noticed that the opposition to Japan was that strong.

[Question] What changes do you foresee in exchange rates?

[Answer] I think the present strong value of the yen simply must be corrected by any means. The self-restraint on auto exports, it has been said, is a bid to gain time for U.S. automakers to make the changeover from producing large cars to producing smaller cars. But has the production of small cars in the United States thereby been made more efficient, and are they competitive? Not at all. In fact, they are less competitive than they used to be.

Even with a stronger yen, productivity in the U.S. manufacturing industries has likewise not improved a bit. Why? Because American companies are already procuring more and more parts from Japan in fields like cars and electronics. With the strong yen, these parts cost more, so the U.S. companies' production costs are going up, not down.

Also, the currencies of the NICs [newly industrialized countries] are tied to the dollar. So the only effect of a stronger yen will be that America will import from the NICs instead of from Japan, with no improvement in the U.S. trade balance.

For America and for the Japanese business community, what we need to seriously consider is: What is really needed for the American economy to regain its international competitiveness?

The Irrational Auto Parts MOSS Conference

[Question] What should be done to relieve economic friction between Japan and the United States?

[Answer] Auto parts have now been added as one of the items on the agenda of the MOSS conference. The assertion over there goes, "Even when American auto parts are cheaper and better, there is around Japanese automakers a thick wall of affiliated parts manufacturers which the American parts industry cannot get into." But the facts are different.

In private conversation with a Commerce Department official I suggested reading MOSS as "More Opportunities to Study and Solve problems"; he agreed.

In other words, we should have a common awareness of the facts. In this connection, I feel there will be three such problems at the next MOSS conference.

First, the question of whether Japanese automobile manufacturers are really striving to buy American-made parts. On this, all of you are making every effort. Second, there is the question of whether American parts manufacturers are maintaining an enthusiastic sales pitch to Japanese automakers. They say they are, but it hardly seems so. Finally, there is the question of who is complaining about what. I think this will have to be shown specifically.

Those are three points we should start from in deepening common perceptions.

[Question] But in considering the MOSS conference process as it has been up to now, I get the feeling that abstract discussions are not something suitable for MOSS.

[Answer] That's quite right. There are no tariff or other systemic barriers affecting auto parts, so they do not fit in with MOSS, which discusses systemic problems.

One thing that should be noted is that precisely because there are many underlying problems, this develops into an emotional issue. So I think we should ascertain not just what appears on the surface of a MOSS conference, but what lies beneath. I think those who are engaged in politics in Japan should make a serious effort to solve these underlying problems.

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END